SUPREME COURT, U. S.

VOLUME 2

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1966

No. 8

CHICAGO AND NORTH WESTERN RAILWAY COMPANY, ET AL., APPELLANTS,

vs.

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, ET AL.

No. 23

UNITED STATES, ET AL., APPELLANTS,

vs.

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY CO., ET AL.

APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF CALIFORNIA

NO. 8—FILED MAY 20, 1965

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[fol. 596]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

ICC Docket No. 31503 and Sub Nos.

Exhibit No. MW-439 (HAM-27)

Witness H. A. Mintz

Transcontinental Divisions

ADDITIONAL TESTIMONY OF H. A. MINTZ

[fol. 597]

Transcontinental Lines' Criticisms
(Exhibits T-299, T-302-305).

Mr. Parr and Mr. Stilling convey the impression that the taper commonly found in rate scales is due (aside from the allowance for terminal service) entirely to merchandising considerations, particularly for the longer distances. Merchandising considerations are of course an important factor in bringing about the taper, but there are two other important factors which contribute to the taper.

In the first place, a rate scale must reflect the fact that there are many expenses which have no relation to the distance a shipment is handled. Examples of such expenses are salaries of general officers and general office expenses. In the second place, a rate scale should, and I believe most scales do, contain an allowance which gives recognition to the fact that a railroad company has a plant and a going organization available to handle traffic day in and day out.

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[fol. 598] This factor is the one to which I referred on cross-examination (Transcript page 2838) as "a standby arrangement." It is obvious that if a railroad company is

to receive compensation reflecting these two factors, they must, generally at least, be reflected in the lower mileage blocks.

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[fol. 599] In his discussion of the minimum primary division of 15 percent proposed by the Eastern lines for two-way breaks and by the Midwestern lines for two, three, and four-way breaks, Witness Stilling states:

> "The purpose of the minimum is to compensate for the terminal services of a short haul carrier under a divisional arrangement based on mileage alone."

I do not agree with this statement. It is true that one of the purposes of the minimum is to compensate a short-haul carrier for terminal service performed. There are, however, other reasons for the minimum.

Provisions for minimum divisions are found in many division sheets covering divisions voluntarily established by the carriers as well as in decisions of the Commission. One of these division sheets is WTL Division Sheet 500-A, which is referred to on page 3 of Mr. Stilling's Exhibit T-304. As is shown on that page, that division sheet provides for a minimum division of 15 percent in addition to containing an inflation of 120 miles as a terminal element. Division Sheet 500-A is still in effect on traffic originating or terminating on the Santa Fe, Union Pacific, Great Northern, Northern Pacific, Denver and Rio Grande Western, and Chicago, Burlington & Quincy.

A minimum primary division should not only cover terminal expense of an originating or delivering carrier, but should also cover other expenses that have no relation to length of haul. Although intermediate carriers do not incur originating or destination terminal expenses, they do

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[fol. 600] incur other expenses that have no relation to the length of haul performed by them. Furthermore, in my opinion, a basis of divisions, like a rate scale, should have

an allowance to reflect the fact that the carrier provides a line of railroad, equipment, and employees to handle traffic day in and day out.

* * * * * * *

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[fol. 601]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

I.C.C. Docket No. 31503, et al

Exhibit No. E-487

Witness L. E. Butler

TESTIMONY

OF

L. E. BUTLER

WITNESS FOR EASTERN RAILROADS

IN ANSWER TO

GILBERT J. PARR—EXHIBITS T-299 TO T-301, T-334

A. J. STILLING—EXHIBITS T-302 TO T-306

H. A. MINTZ—EXHIBIT MW-439

PRIMARY DIVISIONAL BREAK POINTS

DIVISIONAL INTEGER SCALES

AND

SIGNIFICANCE OF GROUP FORM A COST COMPARISONS FOR DIVISIONS

OFFICIAL—TRANSCONTINENTAL DIVISIONS

LEB PRO. 75

* * * * * * *

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[fol. 602] *Application of Fifteen Percent Minimum*

Witness Stilling in Exhibit T-304 discusses the application of a 15 percent minimum in conjunction with integer scales. What he says on page 2 about the first prescribed divisions between Official and Southwestern territories (216 ICC 687, 717) is correct. What he says about the next decision covering Official-Southwestern divisions is partly correct.

That decision applied to and from points in Official territory east of the Illinois-Indiana State Line and did not cover points in Illinois for the very short line-hauls of the Eastern railroads east of East St. Louis-St. Louis. The closest point in Indiana east of East St. Louis is Vincennes, Ind., 147 short-line miles. The integers prescribed in that proceeding produced more than 15 percent for the Eastern railroads for short-line miles of 101 to 150 in the East. The longest short-line mileage block in the Southwest of 1,351 to 1,400 and 51 to 100 in the East produced percents of 85 and 15, respectively. There was no need for a minimum of 15 percent on traffic involving only the Southwestern and Eastern railroads. Those divisions were published in Southwestern Lines' Division Sheet No. 200-A, C.T.R. Division Sheet No. 370, effective April 1, 1940.

That decision also covered traffic moving between Southwestern and Official territories via routes through Southern territory. Several controversies arose between the three groups of carriers regarding the application of that order. One of those controversies related to the minimum percentage for the group of railroads performing terminal

[fol. 603] service. The effective date of the order was postponed until September 1940 accounts. Southwestern lines' Division Sheet No. 201-A was not issued until January 3, 1941, effective with September 1940 accounts, as result of Opinion and Orders of the Interstate Commerce Commission in Dockets Nos. 25692, 25692 (Sub. No. 1), 26429, and 26764. That division sheet provides a minimum

of 15 percent for the Eastern and Southwestern railroads where the prescribed factors for the short-line miles would produce less.

In the Official-Southern Divisions Case, decided July 25, 1939, (234 ICC 175) three sets of factors were prescribed. The factors prescribed in Finding 2 were constructed so as to make a minimum provision of 15 percent unnecessary for the group of carriers having the short haul. Those factors produced 15 percent or more for all short-line miles, except for short-line miles of over 1,000 miles for one group and 50 miles or less for the other group. For all practical purposes those percents were never used, for traffic did not move via the primary break points where the miles north or south were for those distances.

Under Finding 3 the equal factors there prescribed never produced percents less than 15 percent for either group of railroads.

The factors prescribed in Finding 4 applying to Fresh Vegetables from Florida to Official territory produced more than 15 percent for the Eastern railroads' short-line miles. The first factor for the Eastern railroads applied for 250 short-line miles or less.

The Commission Should Prescribe A 15 Percent Minimum For Any Group Of Roads Performing Origin Or Destination Terminal Service.

The Commission has not heretofore limited its prescription of a 15 percent minimum to cases in which it prescribed a mileage prorate. See *Official-Western Trunk Line Divisions,* 269 ICC 765, 786; *Official-Southern Divisions,* 287 ICC 497, 547; *Official-Southwestern Divisions,* 287 ICC 553,

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[fol. 604] 597; *New Jersey & N.Y.R. Co.* v. *the Erie R. Co.,* 292 ICC 479, 485.

Railroad experience indicates that terminal expense is harder to control than line-haul expense, which produces a tendency for terminal costs to rise faster than line-haul

costs. The following table demonstrates that situation. The figures are from Exhibit E-57, page 9.

	Fully-Distributed Box Car Costs			
	Eastern District	Percent of 1947	Western District	Percent of 1947
Year 1947				
Terminal	4.213		4.098	
Line Haul	0.053534		0.047800	
Year 1953				
Terminal	6.128	145.45	5.709	139.31
Line Haul	0.067021	125.19	0.057536	120.37

The same relative situation exists for refrigerator cars. Since the Commission will be fixing divisions for the future, it ought not to skimp on protection of the terminal costs where the Eastern lines having the shorter hauls would suffer most. The Western lines' uniform long hauls help them to absorb their terminal costs.

The 5 percent minimum suggested by Witness Stilling would be almost valueless to the Eastern railroads because under his proposal the Eastern lines for the first mileage block would receive that amount or more for all distances in the West up to 2,250 miles. For 50 miles or less in the East and 2,251 miles and more in the West the percentage to the East would be 4 percent. Appendix E previously referred to adequately illustrates this condition. It will be observed that where the short-line miles in the West are 2,001 to 2,050 the Eastern railroads' short-line miles would have to be greater than 250 miles before the percent East would be 15 percent.

The Missouri-Illinois R.R. example in Witness Stilling's Exhibit T-304, page 10, shows the weakness of the Transcontinental lines' proposal in this respect. At the present

[fol. 605] time the Missouri-Illinois on an average received 4.30 percent and Witness Stilling's 25-mile scale would give the Missouri-Illinois an average of 6.37 percent. The Mis-

souri-Illinois R.R. is a short line serving points in Southern Illinois and, therefore, is not indicative of the rest of Eastern territory. Nevertheless, that railroad performs terminal service on its Transcontinental traffic and is entitled to a fair share of the total revenue instead of a mere pittance of 6 percent.

In Appendix D, previously discussed, I have shown the points in Official territory east of Chicago and East St. Louis to and from which Transcontinental traffic moves, and the short-line mileages east of Chicago and East St. Louis. I have shown the present percents and what the percents would be based on factors in Appendix G to Stilling's Exhibit T-302. It will be seen, as an illustration, that on traffic via Chicago the points located within the 1 to 50-mile block would receive 5 percent of the total revenue. It will also be observed that Witness Stilling would drastically reduce the present percents for Eastern railroads, in some instances by more than one half. A few examples will suffice to show the results.

	Present Percent East	Proposed Percent East
Chicago Heights, Ill.	10	5
Gary, Ind.	13	5
Michigan City, Ind.	13	7
South Bend, Ind.	13	7
Benton Harbor, Mich.	13	7
Kalamazoo, Mich.	13	9
Ft. Wayne, Ind.	13	9
Kokomo, Ind.	13	9
Grand Rapids, Mich.	13	11
Muskegon, Mich.	13	11
Indianapolis, Ind.	13	11

[fol. 606] These examples cover important stations handling Transcontinental traffic through the Chicago gateway. Similar examples could be taken from page 3 of Appendix D covering traffic through East St. Louis-St. Louis.

In considering this showing it is to be remembered that on westbound traffic interchanged at Chicago the Eastern lines absorb the intermediate switching charges of the belt lines used to effect delivery to the Western lines and in many instances their revenue is but slightly more than the amount of the intermediate switching charges.

In Appendix F I have shown examples of traffic taken from the data used in preparing Exhibit E-2, Eastern railroads' traffic study. The revenues and charges shown therein are for October 1953. Under the application of the Stilling factors the revenue remaining for the Eastern railroads in column 9 would have to include both terminal and line haul service. To illustrate, the second example on page 8 covers two cars of Shaving Cream from Hobart, Ind., to Berkley, Calif. The present revenue east of Chicago is $227.44 based on the present division of 13 percent. Witness Stilling's proposal would reduce Eastern lines' division to 5 percent, resulting in Eastern revenue of $87.48 for the two cars. The intermediate switching charges of the belt lines used in effecting delivery to the Western lines is $10.96 per car, or $21.92 for two cars. This amount deducted from $87.48 leaves but $65.56 for the Eastern lines, or $32.78 per car to cover both the origin, terminal, 34 miles of line haul service, and the expense of making delivery to the Western connection through switching line or otherwise. Certainly no one can say that is compensatory revenue east of Chicago for such a substantial service.

On traffic moving via East St. Louis, where a similar showing is made, the percents resulting from Stilling's 25-

[fol. 607] mile scale would not yield adequate revenue for the Eastern lines after paying the transfer charge across the Mississippi River on westbound traffic between East St. Louis and St. Louis. Page 1 of Appendix F shows the

situation on westbound traffic moving via East St. Louis and crossing the river thereat and interchanged with Western lines at St. Louis, Mo. Under the present arrangement the Western lines pay the charges necessary to effect delivery at East St. Louis-St. Louis on both received and delivered traffic to and from Transcontinental territory. The Eastern railroads have proposed that the delivering line assume that expense, which means on westbound traffic they would pay the intermediate charges necessary to effect delivery to the Western lines at East St. Louis or St. Louis. Therefore, I have shown the revenue left for the Eastern railroads after paying the charges out of the revenue east of St. Louis resulting from the Stilling proposal. No one can say that the remaining revenue to the Eastern railroads compensates them adequately for the terminal and road haul service which would be involved.

Appendix 1 of Exhibit E-20 shows the present revenue for the C.&E.I. R.R. on Fresh Fruits and Vegetables from Transcontinental territory to Chicago, Ill., via East St. Louis. In order to show the effect of the Transcontinental lines' proposal based on Stilling's 25-mile block theory, I have prepared Appendix G, attached, showing the revenue results east of East St. Louis and the amounts left for road-haul service for the C.&E.I. R.R. after making the absorptions in the Chicago Switching District. The routing through East St. Louis to Chicago is very important to the Southern Pacific, T.&N.O., and Cotton Belt Railroads and, therefore, the proportions east of East St. Louis on such traffic should be such, based on comparable costs and other considerations, as to give the lines east of East St. Louis

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[fol. 608] sufficient road-haul revenue between East St. Louis and Chicago to warrant participation in the traffic.

This showing adequately demonstrates that the Eastern railroads need a minimum of 15 percent for their short hauls to compensate them for their terminal and road haul service. This can be accomplished in two ways. Design factors that will yield 15 percent for the short hauls in the

East, or provide in the order that the percents resulting from the prescribed factors will be subject to a minimum of 15 percent.

In several divisions cases the Interstate Commerce Commission has prescribed a minimum of 15 percent of the total revenue for the railroads having short hauls in the territory they serve. See *Official-Western Trunk Line Divisions,* 269 ICC 765, 786; *Official-Southern Divisions,* 287 ICC 497, 547; *Official-Southwestern Division,* 287 ICC 553, 597.

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[fol. 609]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Doc. No. 31503 & Sub. Nos.

Exhibit No. MW608 (JKL-1)

Witness: John K. Langum

TRANSCONTINENTAL DIVISIONS CASES

Testimony of

JOHN K. LANGUM

[fol. 610]

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[fol. 612]

QUALIFICATIONS

My name is John K. Langum and I live at 1186 Duncan Avenue, Elgin, Illinois. I am an economic consultant, with my office located at 209 South LaSalle Street in Chicago, Illinois. My work consists of advising and counseling with a wide range of business firms and financial institutions on economic matters of concern to them. Much of my work lies in the field of appraising business conditions and the impact of changing business conditions on particular firms and industries and in the field of interest rates, the money market, and the capital markets. My clients include some of the largest firms and most prominent trade associations in finance, investments, public utilities and industry. In addition to my counseling work, I am a member of the faculty of Indiana University where I am Professor of Business Administration in the School of Business.

In the regular course of my work I am almost continuously engaged in the consideration and analysis of financial statements and financial statistics of a great many individual companies covering the entire range of industries in the American economy.

My educational background includes a B.A. degree received from Colorado College in 1933. In 1936 the University of Minnesota awarded me an M.A. In 1943 the University of Minnesota conferred on me the Ph.D. degree.

I have held several academic positions. From 1935 to 1940 I was on the faculty of the School of Business Ad-

ministration at the University of Minnesota. In 1940 and 1941 I was lecturer in Economics at the University of California. In 1945 and 1946 I was part-time lecturer in the Department of Economics at the University of Chicago. In

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[fol. 613] the summer of 1947, and again in the summer of 1951, I was visiting Professor of Economics at Northwestern University.

Since the spring semester of 1951, I have been on the faculty of the School of Business of Indiana University where I am Professor of Business Administration part-time. I offer a graduate seminar on Analysis of Business Conditions and on the Money and Capital Markets, and I conduct the Finance Forum for the doctoral candidates and faculty in finance.

In addition, I have served on the faculties of several graduate schools sponsored by banking and financial associations. Since 1951, I have been a member of the faculty of the Graduate School of Banking at Rutgers University in New Brunswick, New Jersey, sponsored by the American Bankers Association. Here for two weeks in June of each year I give the courses on the money market and on appraising business conditions for the senior bank officers majoring in commercial banking. Also, I lecture to the entire student body on the business outlook and on interest rates and money markets. Each year about twelve hundred bank officers from most of the forty-eight states and from several foreign countries attend the Graduate School of Banking.

In 1945, I was one of the founders of the School of Banking at the University of Wisconsin, located in Madison, Wisconsin. That school is sponsored by the Central States

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[fol. 614] Conference of sixteen midwestern state banking associations. Since the beginning of the graduate school I have given basic lectures on the money markets. At the School of Banking we have enrolled over one thousand bank officers from about thirty-five states.

Since 1955, I have lectured on appraisal of the economic outlook, analysis of the firm and industry in relation to

changing business conditions, and the structure and workings of the money market at the School of Banking of the South in Baton Rouge at Louisiana State University. This graduate school for bank officers is sponsored by nine southern state banking associations.

Since 1946, over the years I have been a lecturer at the Life Officers Investment Seminar. This is sponsored by the American Life Convention. At the seminar in June each year I have lectured to some one hundred to one hundred and fifty investment officers of the leading life insurance companies of the nation on Treasury and Federal Reserve policies, money and capital markets, and the business outlook.

Since 1948, in August of each year, I have lectured on the money and capital markets and business conditions at the Graduate School of Savings and Loan held at Indiana University, sponsored by the United States Savings and Loan League.

Starting with the session last year, I have lectured on the outlook for growth, the business cycle, and inflation in the American economy, techniques for the analysis of business conditions, and measurement of the impact of

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[fol. 615] changes in the economy on the individual company and industry at the newly formed Financial Analysts Seminar conducted by the National Federation of Financial Analysts Societies in association with the University of Chicago.

My business experience includes employment from 1941 until 1951 by the Federal Reserve Bank of Chicago. From 1944 to 1951 I was Vice President of the bank. As officer in charge of the Research Department during that period, it was my responsibility to direct an extensive research program in monetary and fiscal problems, in the banking mechanism, in business conditions, in agricultural and business economics, and in business finance.

Also at the bank I was in charge of its bank and public relations activities. In addition, for seven years I was Associate Economist of the Federal Open Market Committee

of the Federal Reserve System. This is the body in the Federal Reserve System, made up of members of the Board of Governors and the Presidents of the Federal Reserve Banks, which determines the monetary and credit policies of the nation's central banking system.

Since 1951, I have been engaged in private business as an economic consultant. I am a director of Selected American Shares, Inc., a common stock investment fund with offices in Chicago, Illinois, and of Bankers Mortgage Company of California, a mortgage banking firm with offices in San Francisco, California.

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[fol. 616] I have testified in a number of rate cases before public utility commissions and courts in fifteen states, including Illinois, Indiana, Michigan, Massachusetts, Maryland, Pennsylvania, the District of Columbia, Kansas, Missouri, Kentucky, Montana, Louisiana, Mississippi, Oregon and California. On two occasions, one of which was for the Canadian Pacific Railway Company, I have testified before the Board of Transport Commissioners in Canada.

During the last twenty years I have had many articles published in leading economic and business journals. In 1939, a book of mine was published entitled "Problems and Questions on the Principles of Economics". From 1941 until 1951, I edited "Business Conditions", a monthly review published by the Federal Reserve Bank of Chicago. Since 1946, each year, I have written the articles on banking, including investment banking and commercial banking, on the Federal Reserve System, and other financial subjects for the *Encyclopaedia Britannica Book of the Year*. I prepared the article on savings and savings banking in the United States for the current edition of the *Encyclopaedia Britannica*. During the last year two interviews with me, one on investment policy and the other on the business outlook, were published in "U.S. News & World Report".

I am a member of several professional societies and have been active in many of them and in other professional

activities over several years. In 1949 I was Vice-President

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[fol. 617] for Money and Banking of the American Finance Association. On many occasions I have been on the programs of the National Tax Association, the American Economic Association, and the Investment Analysts Societies. For the last two years I have been chairman of the Elgin Plan Commission in the city in which I live, and I am a member of the American Society of Planning Officials. Since 1955, I have served as Technical Advisor to the Editorial Board of the American Institute of Real Estate Appraisers. Early in July 1957 I accepted an invitation to participate in a Merrill Center Conference for leading experts in the field of economic development of metropolitan areas. Early in June 1957 I testified before the Joint Economic Committee of Congress at their invitation concerning the hearing of the budget outlook and economic situation on growth and inflation in the American economy.

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[fol. 618] GROUPINGS OF RAILROADS

In this divisions case, where comparisons are made among various groups of railroads, the precise composition of the groups is a matter of considerable importance. Unless the composition of the several groups is logical and appropriate, the comparisons made among the groups will not be accurate and meaningful. Accordingly, I have preceded my studies of earning power and financial position by a consideration of proper groupings of the railroads for purposes of such comparisons in this case.

Contending Groups

In these proceedings where conflicting contentions are being put forth primarily by three distinct groups of railroads, I have found that these actively contending groups are of paramount importance in terms of grouping for purposes of comparison. At this point I simply refer to these actively contending groups by the names which ap-

pear to have been quite generally used in the complaints and exhibits which I have seen, viz: Eastern (complainants in Docket 31503), Midwestern (complainants in Docket 31503, Sub No. 1), and Transcontinental (defendants and cross-complainants in both proceedings). I have given emphasis to the financial and related statistics which reveal the relative standing of these actively contending groups and their respective components.

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[fol. 619] It is my understanding that the Chicago, Burlington & Quincy System lines and the Chicago, Milwaukee, St. Paul and Pacific are not members of either of the contending groups, but each of them, individually, is asking for the same bases of divisions as may be prescribed for the Midwestern Group; and that the Louisville and Nashville and the Southern Railroad are in similar manner seeking the same bases as the Eastern Lines. To these last two railroads I have given no special consideration, as I have been advised that their interest is limited to insuring parity with the Eastern Lines in the bases for divisions on transcontinental traffic to and from their stations in Official Territory, which are relatively few.

Neither the Chicago, Burlington & Quincy System nor the Chicago, Milwaukee, St. Paul and Pacific has joined in the presentation of evidence by the Midwestern Group. Yet they are seeking to obtain whatever bases of divisions may be prescribed for the Midwestern Group. Each of them has important mileage in both Mountain-Pacific and Midwestern Territories, and they are among the most important competitors for transcontinental traffic. This situation suggests the propriety of considering all facts which will disclose their true relationships to the two contending groups in the West.

The financial statistics from the annual reports of the Class I railroads in each group, when combined, so closely approximate the results obtainable by including the statis-

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[fol. 620] tics of the smaller roads, that I have omitted the latter in my studies. Had they been included, any differences in resultant group statistics would have been quite

insignificant. For the same reason, I have found it permissible in some instances to omit statistics for some of the smaller Class I railroads, and hence, to include only the predominant or principal Class I roads for certain comparative purposes.

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[fol. 621] *Railroads in Western District*

Problems of grouping and allocation arise in connection with railroads in the Western District. Accordingly, I have listed all Class I line-haul railways in the Western District and the Illinois Central and Gulf, Mobile & Ohio from the Southern District in three tables showing, respectively, the Midwestern Group, the Transcontinental Group, and the railways not in either of such groups. The principal contestants are shown for both the Midwestern and Transcontinental Groups. Brief comment is made as to the nature of control, if the railroad is a subsidiary of one of the principal contestants. These tables are next attached.

TABLE 1

ALL CLASS 1 LINE-HAUL RAILWAYS IN WESTERN DISTRICT
1956

MIDWESTERN GROUP

RAILWAY	Average Miles of Road Operated			
Principal Contestants	Midwestern Territory	Official Territory	Southern Territory	Mountain-Pacific Territory
North Western	9,110			288
Great Western	1,440			
Rock Island	7,580			
Gulf, Mobile & Ohio *	1,050		1,670	
Illinois Central *	3,160	150	3,210	
Minneapolis & St. Louis	1,400			
Soo Line	4,110			57
Missouri-Kansas-Texas	3,220			
Missouri Pacific	9,690			
St.Louis-San Francisco	4,140		590	
Total - Principal Contestants	44,900	150	5,470	345
Other Midwestern Complainants in Class 1				
Duluth, South Shore & Atlantic	540			
Green Bay & Western	220			
Kansas, Oklahoma & Gulf	330			
Lake Superior & Ishpeming	150			
Total - Other Midwestern Complainants in Class 1	1,240			
Total - Midwestern Complainants in Class 1	46,140	150	5,470	345

* From Southern District.

Source: Exhibits MI-424, Appendix L, MI-449, pp. 9, 9B, 11, 11B; Annual Reports of Individual Carriers to Interstate Commerce Commission; Official Guide of the Railways; Interstate Commerce Commission, Bureau of Accounts, Cost Finding and Valuation, Elements of Value of Property, Class 1 Line-Haul Railways Used in Common Carrier Service as of December 31, 1956, February 14, 1958.

TABLE 2

ALL CLASS I LINE-HAUL RAILWAYS IN WESTERN DISTRICT
1956

TRANSCONTINENTAL GROUP

RAILWAY AND NATURE OF CONTROL, IF SUBSIDIARY Principal Contestants	Average Miles of Road Operated Midwestern Territory	Official Territory	Southern Territory	Mountain-Pacific Territory
Santa Fe	9,790*			3,340
Great Northern	4,520			3,550
Northern Pacific	2,770			3,800
Union Pacific	2,860			6,940
Denver & Rio Grande				2,150
Southern Pacific				8,050
Western Pacific				1,190
Total - Principal Contestants	19,940			29,020
Other Transcontinental Defendants in Class I				
Northwestern Pacific - wholly owned subsidiary of Sou. Pac.				330
Sacramento Northern - wholly owned subsidiary of West. Pac.				350
Spokane International - presently being acquired by Union Pacific				150
Spokane, Portland & Seattle - jointly owned by Gr.Northern and Nor. Pacific				950
Total - Other Transcontinental Defendants in Class I				1,780
Total - Transcontinental Defendants in Class I	19,940			30,800

* Borderline mileage in Colorado and New Mexico treated as in Mountain-Pacific territory.

Source: Exhibits MW-424, Appendix L, MW-449, pp. 9, 9B, 11, 11B; Annual Reports of Individual Carriers to Interstate Commerce Commission; Official Guide of the Railways; Interstate Commerce Commission, Bureau of Accounts, Cost Finding and Valuation, Elements of Value of Property, Class I Line-Haul Railways Used in Common Carrier Service as of December 31, 1956, February 14, 1958.

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TABLE 3

ALL CLASS 1 LINE-HAUL RAILWAYS IN WESTERN DISTRICT
1956

RAILWAYS NOT IN MIDWESTERN GROUP OR IN TRANSCONTINENTAL GROUP*

RAILWAY AND NATURE OF CONTROL, IF SUBSIDIARY	Average Miles of Road Operated			
	Midwestern Territory	Official Territory	Southern Territory	Mountain-Pacific Territory
In Midwestern Territory Alone*				
Midwestern Subsidiaries				
Texas & Pacific 78% owned by Missouri Pacific	1,836			
Transcontinental Subsidiaries				
Fort Worth & Denver almost wholly owned by Colo.& Sou.	1,360			
St.Louis-Southwestern 85% owned by Southern Pacific	1,550			
Texas & New Orleans wholly owned by Southern Pacific	4,290			
Independent				
Duluth, Missabe & Iron Range	569			
Kansas City Southern System	1,630			
Texas Mexican	160			
In Mountain-Pacific Territory Alone				
Transcontinental Subsidiaries				
Colorado & Southern 71% owned by C.B.& Q.				720 **
Independent				
Utah Railway				80
Colorado & Wyoming				39 **
In Both Midwestern Territory and Mountain-Pacific Territory				
Transcontinental Subsidiaries				
Chicago, Burlington & Quincy Almost wholly owned by G.N. and N.P.	7,880			890
Independent				
Chicago, Milwaukee, St.Paul and Pacific	7,890	190		2,550

* Excludes Duluth, Winnipeg & Pacific and Toledo, Peoria & Western
**Borderline mileage in Colorado and Wyoming treated as in Mountain-Pacific Territory.
Source: Exhibits MW-424, Appendix L, MW-449, pp. 9, 9B, 11, 11B; Annual Reports of Individual Carriers to Interstate Commerce Commission; Official Guide of the Railways; Interstate Commerce Commission, Bureau of Accounts, Cost Finding and Valuation, Elements of Value of Property, Class 1 Line-Haul Railways Used in Common Carrier Service as of December 31, 1956, February 14, 1958.

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[fol. 625] In addition, the tables show the road mileage in Midwestern Territory, Official Territory, Southern Territory, and Mountain-Pacific Territory. For this present purpose of group and mileage allocations I have treated as Midwestern Territory all of the Western District east of Mountain-Pacific Territory, including Illinois.

Midwestern Group

In the Midwestern Group of complainants the member railroad systems, other than the Illinois Central, the Gulf, Mobile and Ohio and the St. Louis-San Francisco, which have lines in Southern Territory, are located, in practical entirety, in Western Trunk Line and Southwestern Territories. I have noted that the definition of Midwestern Territory in this group's complaint specifically includes all of the Western Trunk Line and Southwestern Territories except North Dakota and northern Minnesota; and in addition, it includes Illinois and a small area in northwestern Indiana adjoining the Illinois portion of the Chicago Switching District.

The ten principal contestants in the Midwestern Group, with 44,900 miles in Midwestern Territory, include: Chicago and North Western System; Chicago Great Western; Chicago, Rock Island and Pacific; Gulf, Mobile & Ohio; Illinois Central; Minneapolis & St. Louis; Minneapolis, St. Paul & Sault Ste. Marie; Missouri Pacific System; Missouri-Kansas-Texas Lines; and St. Louis-San Francisco Lines. When I use the term "Principal Contestants in the Midwestern Group", I refer to these ten roads. Other

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[fol. 626] Midwestern complainants in Class I, four in number, with 1,240 miles in Midwestern Territory, include: Duluth, South Shore and Atlantic; Green Bay & Western; Kansas, Oklahoma & Gulf; and Lake Superior & Ishpeming. When I use the unqualified term "Midwestern Group", I refer to these fourteen railroads, the ten prin-

cipal contestants and the four other complainants in Class I.*

As indicated, the aggregate mileage of the Midwestern Group is about 46,140 in Midwestern Territory. These railroads have no mileage in Mountain-Pacific Territory with the exception of the Chicago and North Western and the Minneapolis, St. Paul & Sault St. Marie. The former has a 288-mile stub-end line extending westward from the Nebraska line to Lander, Wyoming in Mountain-Pacific Territory. The latter has 57 miles in Montana. Additionally, the Illinois Central has 3,210 miles, the Gulf, Mobile and Ohio has 1,670 miles and the St. Louis-San Francisco Lines have 590 miles, in Southern Territory. The Illinois Central also has 150 miles in Official Territory.

Transcontinental Group

Four members of this group are located partly in Midwestern Territory and partly in Mountain-Pacific Territory. These railroads are: Atchison, Topeka and Santa

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[fol. 627] Fe; Great Northern; Northern Pacific; and Union Pacific. In total, these railroads have 19,940 miles in Midwestern Territory and 17,630 miles in Mountain-Pacific Territory.

The Santa Fe extends from the Pacific Coast to Chicago, while these other three overlapping or split roads extend from the Coast with their own railroads to the Twin Cities and to Missouri River points. However, the Great Northern and Northern Pacific, together with their jointly owned subsidiaries, the Spokane, Portland and Seattle and the Chicago, Burlington & Quincy, form through transcontinental routes to Chicago and other eastern and southern gateways. They are now engaged in studies the expressed

* The Midland Valley and the Oklahoma City-Ada-Atoka, members of the Midwestern Group, were Class I railroads until 1956, when the Commission's change in the classification rule shifted them to Class II (less than $3,000,000 annual gross revenue). Another member, Minneapolis, Northfield and Southern, was not included as a Class I line-haul carrier until 1956.

object of which is "to determine whether or not it would be advantageous to merge their systems" with these jointly owned subsidiaries (Northern Pacific, Annual Report to Stockholders, 1956, p. 12). A more recent statement by the President of the Great Northern indicates the hope and expectation that a proposal for such a merger will be filed with this Commission "by the end of the year" (*Wall Street Journal,* May 8, 1958).

Notwithstanding its much greater mileage in Midwestern Territory, the Atchison, Topeka & Santa Fe "joined with the other interested railroads of the West in a common defense of the present divisions of revenue which are believed to be fair and reasonable to the complaining carriers and in some respects unfair to the West.". (See Annual Report to Stockholders, 1954, pp. 16-17). In the 1954 an-

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[fol. 628] nual reports to stockholders other prominent members of this group expressed the common purpose to "defend" the existing bases of divisions. (See Southern Pacific, p. 6; Northern Pacific, p. 11; Western Pacific, p. 22; Union Pacific, p. 28). Accordingly, in all groupings which have come to my attention the Santa Fe has been included in the Transcontinental or Mountain-Pacific groups.

In addition to these four overlapping or split roads, there are three other prominent members of the Transcontinental Group with mileage only in Mountain-Pacific Territory. These include: Denver and Rio Grande Western; Southern Pacific (including its leased lines); and Western Pacific. When I use the term "Principal Contestants in the Transcontinental Group", I refer to these seven roads.

The four other Transcontinental defendants in Class I are smaller roads, all subsidiaries, wholly- or almost wholly-owned, of certain Principal Contestants in the Transcontinental Group. These four railroads, with a total of 1,780 miles located entirely within Mountain-Pacific Territory, are: Northwestern Pacific; Sacramento Northern; Spokane International; and Spokane, Portland & Seattle.

When I use the unqualified term "Transcontinental Group", I refer to this group of eleven actively contesting railroads, the seven principal contestants and the four other defendants in Class I. These were all named as de-

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[fol. 629] fendants in the complaints of the Eastern and Midwestern Groups. In total, the Transcontinental Group has 30,800 miles in Mountain-Pacific Territory. In addition, as previously noted, the four split or overlapping railroads have 19,940 miles in Midwestern Territory. The Transcontinental Group so constituted is the same as that which I understand has been used by Witness Kleinsorge in the Midwestern Group's statistical exhibits introduced through him, such as MW-86, wherein the make-up of the defendant Transcontinental Group is set forth.

Railways Not in Midwestern Group or in Transcontinental Group

All remaining Class I line-haul railways in the Western District not included in either the Midwestern Group or in the Transcontinental Group are listed in the final table of railroad groupings. (Table 3)

Seven such railroads serve Midwestern Territory alone. The single subsidiary of a member of the Midwestern Group is the Texas and Pacific, 1,836 miles in length, located wholly within Midwestern Territory. The Missouri Pacific holds 78 percent of its capital stock.

Three subsidiaries of members of the Transcontinental Group operate in Midwestern Territory alone. The Fort Worth & Denver, owned by and an extension through Texas of the Colorado & Southern, a subsidiary of the Chicago, Burlington & Quincy, in turn a subsidiary of the Great Northern and the Northern Pacific, has 1,360 miles.

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[fol. 630] The St. Louis-Southwestern, 88 percent owned by the Southern Pacific and constituting the eastern component of the Southern Pacific System's so-called Cotton Belt Route to East St. Louis, has 1,550 miles. The Texas & New Orleans, with 4,290 miles, is a wholly-owned sub-

sidiary of the Southern Pacific Company, constituting the eastern component of the Southern Pacific System's so-called Sunset Route to New Orleans and an intermediate component of its Cotton Belt Route.

Three remaining Class I railroads in Midwestern Territory alone are independent, not being closely associated with members of either the Midwestern or the Transcontinental Groups through complete or majority ownership of securities. The Duluth, Missabe & Iron Range has 569 miles. It is neither complainant nor defendant in this case. The Kansas City Southern System, including the Louisiana & Arkansas, is an independent north and south line extending from Kansas City to Gulf of Mexico ports, with 1,630 miles of road. The Texas Mexican is a small independent line 160 miles long near the Mexican border.

The Toledo, Peoria & Western and the Duluth, Winnipeg & Pacific are listed by the Commission as roads in the Western District. These I have accounted for in the Table 3 footnote. The former is located in Illinois, is jointly controlled by the Santa Fe and the Pennsylvania Railroads, and is a member of the Eastern complainant group. The latter is a wholly-owned appendage of the Canadian National Railways System. It extends from Fort Francis, Ontario, to Duluth, Minnesota, with 169 miles in the United States.

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[fol. 631] Three Class I railroads, not in either the Midwestern Group or in the Transcontinental Group, operate in Mountain-Pacific Territory alone.

The Colorado & Southern, a subsidiary of the Chicago, Burlington & Quincy, has about 720 miles of road running in a northerly and southerly direction along and adjacent to the eastern boundary of Mountain-Pacific Territory. Much of its mileage is used to define the boundary in Colorado. Mr. Bearss included it in his Mountain-Pacific Group as a Class I road serving that territory (Exhibit T-238, p. 19). It is not a member of either actively contending group, it having joined in the Chicago, Burlington & Quincy complaint. Hence, its statistics are not reflected in any of the

Transcontinental Group's statistics to be used by me. Even had they been so reflected, the results would not have been materially affected. For example, the 1951-6 average group rate of return, unadjusted, on the ICC Elements of Value basis would have been unaffected; and the fully adjusted group rate of return would have been reduced by 3/100ths of one percentage point (.03%).

The Utah Railway, owned by United States Smelting & Refining Co., is a 99 percent coal carrying railroad having ownership in some 80 miles of trackage, plus operating rights, all in Mountain-Pacific Territory. It is also included in Exhibit T-238, Group 3. It has not been a Class I railroad since 1955. (Moody's Transportation Manual,

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[fol. 632] 1957) Its participation in transcontinental traffic is "inconsequential". (See Exhibit T-244, Appendix B, p. 53, Witness F. C. Nelson.)

Another small railroad, the Colorado & Wyoming, is owned by the Colorado Fuel & Iron Co. and has some 39 miles of main tracks located in Colorado and Wyoming along and adjacent to the eastern boundary of Mountain-Pacific Territory. It likewise is included in Exhibit T-238, Group 3, but not in my Transcontinental Group. I am advised that it is a negligible participant in transcontinental traffic movement.

These last two railroads were named as defendants in the complaint of the Eastern Railroads but not in the complaint of the Midwestern Group. It is found that the inclusion or exclusion of the annual statistics for these two small railroads in setting up rate of return statistics for the Transcontinental Group makes no differences in the resultant group percentages as great as 1/100th of a percentage point (.01%). For these reasons the consist of statistics for the Transcontinental Group to which I shall refer does not include the statistics of these two small roads.

Two other large railroads, not members of either the Midwestern Group or the Transcontinental Group, operate in both Midwestern Territory and Mountain-Pacific Terri-

tory. These are the Chicago, Burlington & Quincy and the Chicago, Milwaukee, St. Paul and Pacific.

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[fol. 633] *The Burlington*

The situation of the Chicago, Burlington & Quincy System requires special consideration. It has 7,880 miles in Midwestern Territory and 890 miles in Mountain-Pacific Territory. Notwithstanding its much larger mileage in Midwestern Territory, it has not joined the Midwestern Group of complainants. Its complaint is non-aggressive in nature, which is quite understandable in view of its practically complete ownership and control by the Great Northern and Northern Pacific. These two prominent members of the Transcontinental Group own, in equal shares, 99 percent of the capital stock of the Burlington. Between these three there is an obvious unity and continuity of interest which is allied with the contending Transcontinental Group. Taken together they already constitute an affiliated transcontinental railroad system extending from the Pacific Coast to Chicago and other eastern connecting points. Except for the presently intervening corporate structures and separate operations, theirs is a situation similar to that of the Atchison, Topeka and Santa Fe, which extends entirely across Midwestern Territory to eastern gateways and has roughly three-fourths of its mileage therein.

The Milwaukee

The physical situation of the Chicago, Milwaukee, St. Paul and Pacific, commonly called "the Milwaukee", has

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[fol. 634] similarity to those of the Santa Fe and the Great Northern-Northern Pacific-Burlington combination in that its railroad extends from the Pacific Coast to Chicago and other junctions with Eastern Railroads. It has about 7,890 miles in Midwestern Territory, 2,550 miles in Mountain-Pacific Territory, in an extension from the Montana-North

Dakota border to the Pacific Coast, and 190 miles in Official Territory. However, important other circumstances indicate, if the Milwaukee is to be included with any group, that it would be more appropriately placed with the Midwestern Group. It is notable, first, that it is independent of any ownership or control by members of the Transcontinental Group, or otherwise. This completely independent railroad has its greatly predominant mileage in Midwestern Territory. Its geographical location evidently places it in a position to receive benefit from increases in Midwestern divisional bases if made applicable to it, for, in contradistinction to the Santa Fe, its management has expressed itself as being "thoroughly in accord with the position of the Western Trunk Line carriers that their present divisions on transcontinental traffic are inadequate". (See Exhibit MW-439, Witness Mintz, pp. 56-57).

Importance of Contending Groups in Proper Comparisons

The various situations of ownership and control to which I have referred are important for consideration in setting up groups of railroads for purposes of statistical comparison. This is particularly true when comparing

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[fol. 635] earning power and financial standing in relation to revenue needs and the importance of adequate transportation services to the public.

The geographical situation of the Midwestern Group and its subsidiaries and the Transcontinental Group and its subsidiaries exposes the impossibility of considering either of these two contending groups of western railroads as serving, exclusively, a specific territory. The approximate road mileage in Midwestern Territory of the Transcontinental Group, 19,940, and that of its subsidiaries (Chicago, Burlington & Quincy, Fort Worth & Denver, St. Louis-Southwestern, and Texas & New Orleans), 15,080, aggregates 35,020. These mileages compare with 30,800 miles in Mountain-Pacific Territory of this same Transcontinental Group and 1,610 miles of Mountain-Pacific mileage of sub-

sidiaries, a total of 32,410. In contrast, road mileage in Midwestern Territory of the Midwestern Group is 46,140 and that of subsidiaries is 1,836, a total of 47,976 miles. Total road mileage in Mountain-Pacific Territory of the Midwestern Group is only 345 miles, with no such mileage for the single Midwestern Group subsidiary.

Furthermore, any attempt to group territorially all western railroads, without regard to their respective positions in this case, meets with difficulties which make such classification inappropriate and less meaningful than that of the contending groups. Through their securities owner-

[fol. 636] ship of four of the six principal railroads outside of the Midwestern Group in Midwestern Territory, three of the Transcontinental Group control those companies which operate by far the greater part of the Midwestern railroad mileage outside of the Midwestern Group. These four subsidiaries of Transcontinental Group railroads have approximately 15,080 miles in Midwestern Territory and are wholly within that territory except for 890 miles of road of the Burlington in Mountain-Pacific Territory. The 720 miles of road of the Colorado & Southern are on and adjacent to the eastern boundary of Mountain-Pacific Territory. Thus the subsidiary companies of the Great Northern, Northern Pacific, and Southern Pacific operate more than 15,000 Midwestern miles in contrast with approximately 11,500 miles operated by other Class I western roads outside the Midwestern Group. Of these other railroads, the Chicago, Milwaukee, St. Paul & Pacific accounts for 7,890 miles in Midwestern Territory.

In direct proportion to their respective stock ownerships, these Transcontinental owners derive the benefits of whatever earnings accrue from their Midwestern subsidiary railroad operations. Although such earnings are not directly reflected as income in the accounts of the parent companies until received as dividends (and then not as income from railroad operations), this very large control and ownership of the most important competitors of the

Midwestern Group in Midwestern Territory appeals to me

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[fol. 637] as a highly significant fact. It seems quite apparent that in the event of a shrinkage in Transcontinental Group's revenues due to the granting of increases in divisions throughout Midwestern Territory, there would be a substantial offsetting effect because of resultant increases in revenues of these subsidiary railroads. Given that these subsidiaries have these close relationships to the Transcontinental Group and that they have taken no position as to the adequacy of their present divisions, I fail to see any justification for including them in any "Midwestern" group; and I have not done so.

The varying situations which I have outlined appear to me to preclude any logical or reasonable all-inclusive grouping of the western railroads along territorial lines for purposes of comparison as to earning power, financial condition, and related matters. As already mentioned, Mr. Bearss made some attempts along that line. I have noted that some of his groupings were adopted by Dr. Edwards and others by Mr. Lovett. For the reasons already stated, I cannot agree that these groupings are appropriate or meaningful. For convenience, nevertheless, I shall use the territorial names, "Midwestern" and "Transcontinental", as obviously useful means of reference to the two groups of western railroads who are making conflicting contentions in these proceedings. It is the relative standing of these two actively contending groups, as specifically defined above in terms of their respective positions in this case, which has fundamental significance.

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EARNING POWER AND RATE OF RETURN COMPARISONS IN TERMS OF GROUP TOTALS

The studies which I have made of earning power and rate of return include several sets of comparisons. First, I have studied earning power before taxes as related to total operating revenue, to net investment in terms of the

I.C.C. valuation base, and to net investment in terms of the book value base. Similarly, I have related earning power after taxes to these three magnitudes. Finally, I have studied rates of return on both types of net investment base.

These studies have been made basically in terms of the contestant groups in this case. Consideration has also been given to an alternate comparison where figures for the Milwaukee Road have been added to the Midwestern Group. Likewise consideration has been given to the principal contestants, in terms both of group totals and of averages of individual ratios. Attention has been given to earning power and rate of return data for the groupings used by Mr. Bearss and to what I consider distortions in the comparisons he has presented.

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[fol. 639] *Earning Power before Federal Taxes*

The first comparisons I make are those of "Earning Power Before Federal Taxes". In the series of tables so entitled, I have shown such statistics for the eleven postwar years, 1946 through 1956. These data provide an excellent measure of what might be termed raw or gross earning power of the several groups, without regard to the different Federal tax situations of the particular railroads. The group designation is shown in Column (1) and in parallel columns the group averages are separately stated for the eleven-year period as a whole (Column 2), for the first five of those years (Column 3), and for the last six of those years (Column 4). Figures are set forth in the last column (Column 5) which indicate the relationship of the average for the last six years, 1951-56, to that for the first five years, 1946-50. In addition to the tables, a chart is presented for each aspect of comparison, showing the most important relationships.

Data for the year 1957 became available earlier this year, and earning power and rate of return computations using these data have been completed in recent weeks. Compari-

sons for the year 1957 are shown in a separate table following that presenting the corresponding comparisons for the years 1946 through 1956.

Ratio of Pretax Net Railway Operating Income to Total Operating Revenue

Chart I, Table 4, and Table 5, display the group ratios of net railway operating income before Federal taxes to total operating revenues. In other words, this is the percent of operating revenue remaining after payment of all operating expenses, rents, and taxes other than Federal income and excess profits taxes. As the caption in Chart I

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[fol. 640] and the first sub-heading in the tables "Contestant Groups", indicate, the groups there compared are the three contending groups of Class I railroads which I have described. Reference to Chart 1 indicates that the Transcontinental Group stands out as realizing, quite substantially, the highest portion of revenue remaining before Federal taxes. For instance, in the 1951-56 period the ratio of pretax net railway operating income to total operating revenue was 16.45 percent for the Transcontinental Group, 29 percent more than the 12.72 percent ratio for the Midwestern Group. The corresponding percentage of excess had been about 21 percent in the 1946-50 period. Thus the advantage in pretax earning power which the Transcontinental Group enjoyed over that of the Midwestern Group increased from the first five postwar years to the last six postwar years.

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[fol. 641] *Rate of Return on I.C.C. Valuation Base*

The data in Chart VII, Table 16 and Table 17 show, for the 1951-56 period, rate of return comparisons in terms of the ratio of net railway operating income to net investment as measured by the I.C.C. valuation base.

The unadjusted rate of return was 4.68 percent for the Transcontinental Group, 3.89 percent for the Eastern

Group, and 3.76 percent for the Midwestern Group. Thus the unadjusted rate of return for the Transcontinental Group was 25 percent in excess of that for the Midwestern Group. In the alternate comparison, it was 33 percent greater.

After the combined adjustments, the rate of return was 4.59 percent for the Transcontinental Group, 3.62 percent for the Eastern Group and 3.42 percent for the Midwestern Group, Thus the fully adjusted rate of return for the Transcontinental Group was 34 percent greater than that of the Midwestern Group. The fully adjusted rate of return for the Eastern Group was 6 percent greater than that of the Midwestern Group.

In the alternate comparison, with the Milwaukee included, the rate of return after both adjustments drops to 3.18 percent for the Midwestern Group. On this basis, the rate of return of the Transcontinental Group exceeded that of the Midwestern Group by 44 percent. Similarly, the rate of return for the Eastern Group was in excess of that of the Midwestern Group by 14 percent.

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[fol. 642] The substantial margin by which rate of return for the Transcontinental Group and the Eastern Group exceeded that of the Midwestern Group continued to be evident in 1957. The fully adjusted rate of return, related to the I.C.C. valuation base, was 38 percent greater for the Transcontinental Group and 24 percent greater for the Eastern Group. In the alternate comparison, with the Milwaukee added to the Midwestern Group, the excess was 43 percent for the Transcontinental Group and 28 percent for the Eastern Group. In terms of principal contestants, the superiority of the Transcontinental railroads was 40 percent.

These data on rate of return relate net railway operating income after adjustment for both tax matters to net investment on the I.C.C. valuation base. In my judgment, these data are the most meaningful of all these measurements. Accordingly, I regard the data presented in Chart VII, Table 16, and Table 17 as the most significant

comparison of the relative earning power of the contestant groups in this divisions case.

Rate of Return on Book Value Base

Rate of return comparisons in terms of the ratio of net railway operating income to net investment on the book value base are shown in Chart VIII, Table 18, and Table 19.

For the 1951-56 period the unadjusted rate of return averaged 3.94 percent for the Transcontinental Group, 3.75 percent for the Eastern Group, and 3.60 percent for the Midwestern Group. Thus the unadjusted rate of re-

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[fol. 643] turn, even on the book value basis, for the Transcontinental Group exceeded that of the Midwestern Group by 9 percent.

The fully adjusted rate of return was 3.87 percent for the Transcontinental Group, 3.48 percent for the Eastern Group, and 3.27 percent for the Midwestern Group. Thus the rate of return after the combined adjustments was 18 percent higher for the Transcontinental Group than that of the Midwestern Group. In the alternate comparison, the excess was 27 percent.

The superiority of rate of return, even when related to the book value base of net investment, continued during 1957. As shown in Table 19, the rate of return, so measured, after combined adjustments, was 23 percent greater for the Eastern Group and 19 percent greater for the Transcontinental Group.

Earning Power and Rate of Return Comparisons in Terms of Averages of Individual Ratios

The comparisons of earning power before Federal taxes, earning power after Federal taxes, and rate of return presented in Tables 4 through 19 are in terms of aggregates of figures for the contestant groups of railroads, the groups of railroads in the alternate comparisons, and the principal contestants in the Western District. Another approach to this type of comparisons is in terms of averages

of individual ratios for the principal roads in the several contestant groups. Such comparisons of earning power before Federal taxes, earning power after Federal taxes, and rate of return are presented in the series of tables which

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[fol. 644] follow on pages 74 through 93. These comparisons in effect weight the individual roads equally as individual enterprises making up the contestant groups. These tables are organized in parallel fashion to the previous tables. However, in this series the 1957 figures are included, with the figures for the earlier years, on a single page instead of being shown on an additional page. For instance, Table 20 shows data for the years 1946-56, 1946-50, 1951-56, and 1957 on earning power before Federal taxes as measured by the ratio of pretax net railway operating income to total operating revenue. Data in terms of aggregates which correspond to these data in terms of averages of individual ratios are presented in Tables 4 and 5. Again, as additional examples, Table 21 corresponds to Tables 6 and 7, Table 22 corresponds to Tables 8 and 9, and so on.

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[fol. 645] *Principal Railroads*

The principal railroads for which data are shown in Tables 20-29 are those listed earlier in my discussion of groupings of railroads. The seven principal railroads in the Eastern Group, studied by Mr. Bearss (Exhibit T-275), by Mr. Boles (Exhibits T-336 through T-349), and in part by Mr. Jansen (Exhibit E-396), include: Baltimore and Ohio; Chesapeake and Ohio; Erie; New York Central; New York, Chicago & St. Louis; Pennsylvania; and Wabash.

The ten principal Midwestern systems, listed in Table 1, include: North Western; Great Western; Rock Island; Gulf, Mobile & Ohio; Illinois Central; Minneapolis & St. Louis; Soo Line; Missouri-Kansas-Texas; Missouri Pacific; and St. Louis-San Francisco.

The seven principal contestants in the Transcontinental Group, listed in Table 2, include: Santa Fe; Great North-

ern; Northern Pacific; Union Pacific; Denver & Rio Grande; Southern Pacific; and Western Pacific.

Lower Earning Power of Midwestern Group

In terms of each of the comparisons of earning power, whether before or after Federal taxes, the average for the ten principal Midwestern systems is less than that for the seven principal Eastern railroads, which in turn is lower than that for the seven principal Transcontinental roads. In terms of the first ratio, for instance, as shown in Table 20, earning power before Federal taxes as measured by the ratio of pretax net railway operating income to total

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[fol. 646] operating revenue during 1951-56 averaged 13.24 percent for the ten Midwestern systems, 14.07 percent for the seven Eastern roads, and 17.98 percent for the seven Transcontinental roads. The same ratio in 1957 averaged 9.32 percent for the ten Midwestern systems, 10.69 percent for the seven Eastern roads, and 15.30 percent for the seven Transcontinental roads.

Lower Rate of Return of Midwestern Group

When adjustment is made for both tax matters, (1) by excluding income tax on non-operating income and (2) by removing the effect of tax deferrals as a result of rapid amortization, we obtain normalized rate of return comparisons.

The most significant and meaningful rate of return comparison, as previously noted, is that which relates net railway operating income, after both tax adjustments, to the I.C.C. elements of value base. Such a comparison is shown for the years 1951-1956 in Table 26. During this period, the rate of return, by this measure, averaged for the individual ratios of the seven principal Transcontinental Roads 4.68 percent, 38 percent greater than the 3.39 percent average for the ten principal Midwestern systems. The rate of return averaged 4.61 percent, in this approach, for the seven individual Eastern roads which have been

characterized as the principal roads in Official Territory. This was 36 percent greater than the average for the ten principal Midwestern systems.

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[fol. 647] Corresponding rate of return data on the I.C.C. valuation base are shown for 1957 in Table 27. In the year 1957 the rate of return, by this measure, averaged 3.93 percent for the seven principal members of the Transcontinental Group, 3.90 percent for the seven principal Eastern roads, and 2.58 percent for the ten principal members of the Midwestern Group. The average rate of return for these Transcontinental roads exceeded that of the Midwestern system by 52 percent. Similarly, the average rate of return for these Eastern roads exceeded that of the Midwestern system by 51 percent. Similar results are shown in Tables 28 and 29 where the book value base is used for computing rate of return.

These comparisons of earning power and rate of return in terms of averages of individual ratios for the principal members of the contending groups present a different view than that in terms of aggregate figures. Nevertheless, by this approach, as well, the superior earning power of the Transcontinental Group, particularly, and the lesser earning power of the Midwestern Group are manifestly clear.

Earning Power and Rate of Return Comparisons in Terms of Bearss' Groupings

Two groups were used by Mr. Bearss in his testimony as representing midwestern roads. The next set of these same indicators of earning power and rate of return will show the answers obtainable for the groups as selected and constituted by Mr. Bearss. Alternate comparisons will be made to show the effect of certain changes in his groupings on these measures of earning power and rate of return.

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[fol. 648] *Midwestern Groups*

In Exhibit T-238 (p. 19) Mr. Bearss used a group which he termed "Midwestern Group—All Roads". In this cate-

gory he included the members of the Midwestern Group, as listed in Table 1 of my testimony, but in addition he included all other Class I railroads in the Western District except the four overlapping Transcontinental roads, the Milwaukee Road, and the ten roads which operate exclusively in Mountain-Pacific Territory. The effect of this selection, of course, was to combine diverse roads into one category. The four Transcontinental subsidiaries in Midwestern Territory (CB&Q, Ft.W&D, St.L-SW, and T&NO) and other Class I railroads having mileage in Midwestern Territory, with the exceptions noted, were thus joined in one group with the Midwestern complainants as though their interests were as one.

In Exhibit T-275 (p. 1) Mr. Bearss used a group which he termed "Principal Midwestern Roads". In this category he included these Transcontinental subsidiaries (except the Fort Worth & Denver), the Texas & Pacific, and four of the Midwestern complainants, viz: North Western, Rock Island, Missouri Pacific, and Illinois Central.

In each of these exhibits Mr. Bearss included in his "Mountain Pacific" group not only the seven Principal Transcontinental Contestants but also the Milwaukee. In addition, in Exhibit T-238, the lesser Transcontinental Group roads (Northwestern Pacific, Sacramento Northern, Spokane International, and Spokane, Portland & Seattle)

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[fol. 649] were also included in his "Mountain-Pacific" group as well as other railroads operating in Mountain-Pacific Territory alone (Colorado & Southern, Utah Railway, and Colorado & Wyoming).

Ratios for the Bearss' Groupings

For reasons already indicated, I consider such groupings to be inappropriate. Nevertheless, the favorable position of the Transcontinental Group is evident in the data for the groupings precisely as selected and constituted by Mr. Bearss. In Tables 30-45 there are shown, under the headings "Bearss' All Roads (T-238)" and "Bearss' Prin-

cipal Roads (T-275)" the ratios of these midwestern and mountain-pacific groups. All the measures of earning power and rate of return previously shown for the contestant groups and principal contestants are shown for Mr. Bearss' groupings. Tables 30-45 thus correspond to Tables 4-19.

These data show, even in terms of Mr. Bearss' groupings, the higher level of earning power and rate of return of the mountain-pacific over the midwestern railroads and the marked improvement during recent years in their favorable situation. Alternate comparisons are then made, to move towards more appropriate and meaningful categories, to show the effect of certain changes in his groupings. These relate particularly to more appropriate grouping of the Milwaukee and treatment of the Transcontinental subsidiaries.

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[fol. 650] *Lower Earning Power of Midwestern Group.*

For instance, the ratio of pretax net railway operating income to total operating revenue is presented in Tables 30 and 31 as a measure of earning power before Federal taxes. These tables, for the Bearss' groupings and alternate comparisons, correspond to Tables 4 and 5 for the contestant groups and principal contestants. As seen in Table 30, in the case of the "All Roads" comparison, the ratios in the midwestern and mountain-pacific groups as used by Mr. Bearss are very close to being identical in the average for the 1946-56 period as a whole. The mountain-pacific was 6.6 percent less than the midwestern for the first five years and 4.2 percent greater during the last six years of the period. Going on to Table 31, where results for 1957 are shown, this ratio for earning power before taxes was 15.5 percent greater for the Bearss' Mountain-Pacific group than for his Midwestern group. In Tables 30 and 31 immediately below this first comparison is shown Alternate Comparison I, in which the Milwaukee is shifted from mountain-pacific to midwestern. This results in a

mountain-pacific ratio 11.7 percent higher than the midwestern for the 11-year period, 4.6 percent greater in the first five years and 16.9 percent greater in the last six years. The 1957 results show an excess of 46 percent for the mountain-pacific group, with the Milwaukee shifted to the midwestern.

In Alternate Comparison II, in addition to the more appropriate position of the Milwaukee, the four Transcontinental subsidiaries and the DM&IR have been taken out of the midwestern group. The resultant ratios indicate

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[fol. 651] the percentage of excess of mountain-pacific over midwestern to be as follows: 1946-56, 24.3 percent; 1946-50, 19.7 percent; 1951-56, 27.4 percent; 1957, 39.1 percent.

As regards the Bearss "principal roads" groupings, it can be seen from the last three comparisons on Tables 30 and 31 that similar results are developed. Taking first the groups as Mr. Bearss selected them, the mountain-pacific advantage was 2.4 percent for the 11-year period notwithstanding a disadvantage of 4.6 percent in the first five years. This is because the disadvantage was reversed and became an advantage of 7.7 percent in the last six years. In 1957 the excess of earning power before taxes for the mountain-pacific principal roads, as grouped by Mr. Bearss, amounted to 25 percent.

Alternate Comparisons III and IV, in relation to these Exhibit T-275 groupings, show that on the "principal roads" basis (1) when the Milwaukee is transferred to the midwestern category (Comparison III) and, (2) when it is so transferred and the Transcontinental subsidiaries are excluded from that category (Comparison IV), the percents of excess in this earning power factor of the mountain-pacific roads in comparison with the midwestern roads again increase very substantially. As is shown on the bottom line of Tables 30 and 31, in Alternate Comparison IV, the superiority of the mountain-pacific group so constituted was 29.2 percent in 1946-50, 39.5 percent in 1951-1956, and 52.9 percent in 1957.

Similar results appear in the remaining tables in this series on earning power, where the other factors both before and after taxes are shown (Tables 32 through 41).

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[fol. 652] *Lower Rate of Return of Midwestern Group*

Reference is now made to the most significant measure of rate of return, shown on Tables 42-43. This is the ratio of net railway operating income after the combined adjustment for tax effects to net investment on the I.C.C. valuation base. The comparisons again cover the period 1951-56 and the year 1957. Even on the basis of the "all roads" groupings used by Mr. Bearss in Exhibit T-238, this rate of return for the mountain-pacific group exceeded that of the midwestern group by 9.5 percent in the period 1951-56 and by 15.2 percent in 1957. In Alternate Comparison II, with the Milwaukee shifted to the midwestern group and the Transcontinental subsidiaries excluded, the excess of the mountain-pacific group so constituted was over 33.4 percent in 1951-56 and 31.7 percent in 1957.

On the basis of the "principal roads" groupings used by Mr. Bearss in Exhibit T-275, this rate of return for the mountain-pacific group exceeded that of the midwestern group by 12.7 percent in 1951-56 and 20.4 percent in 1957. In Alternate Comparison IV, the excess was 44.5 percent in 1951-56 and 38 percent in 1957.

These trends as to earning power and rate of return are shown throughout Tables 30-45. From the comparisons here presented, confirmation is found as to the advantage in earning power of the Transcontinental Group, the improvement relative to the Midwestern Group in 1951-56 over 1946-50, the further progress relative to the Midwestern Group in 1957, and its still greater advantage when more appropriate treatment is given the Milwaukee and the Transcontinental subsidiaries.

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EARNING POWER AND RATE OF RETURN SUMMARY

Comprehensive Comparisons

Measurements from several standpoints have been included in the studies which I have made of earning power and rate of return. Efforts have been made to utilize all commonly used concepts of net railway operating income, the bases to which these magnitudes are related, and methods of averaging the ratios derived.

In terms of income concepts, the data concerning earning power before taxes use net railway operating income before Federal taxes, while the series on earning power after taxes employs net railway operating income adjusted by adding back Federal taxes on non-operating income. The rate of return data make use of unadjusted net railway operating income, net railway operating income adjusted by adding back Federal taxes on non-operating income, net railway operating income adjusted for the effect of tax deferrals resulting from rapid amortization, and net railway operating income after both adjustments. In terms of the bases to which these income concepts have been related, in all series of comparisons, net investment is shown on both the I.C.C. valuation base and the book value base. In terms of combining the data derived, the measurements in charts I-VIII, Tables 4-19, and Tables 30-45 are based on group totals of the underlying figures, while the measurements in Tables 20-29 are based on simple arithmetic averages of the individual ratios. Data are presented in terms of all roads in the several groups and also in terms of the principal roads in such groups. Consideration is

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[fol. 654] given as well to alternate groupings, including those used by witnesses for the Transcontinental and Eastern railroads.

Preponderant Advantage Over Midwestern Group

In terms of the several earning power and rate of return comparisons between contestant groups, the ratios for the Transcontinental Group exceeded those for the Midwestern Group by percentages which ranged from +10.6 percent to +41.8 percent in the 1946-50 period, from +18.3 percent to +51.7 percent in the 1951-56 period, and from +19.4 percent to +74.2 percent in the year 1957. While the ratios for the Midwestern Group exceeded those for the Eastern Group in the early postwar period, in the later and more significant years the opposite has been true. The ratios for the Eastern Group exceeded those for the Midwestern Group by percentages which ranged from +1.4 percent to +7.3 percent in the 1951-56 period, with the exception of a single comparison which came out to —0.4 percent. In the year 1957, the range was from +12.8 percent to +33.8 percent.

Similar results appear in terms of the several comparisons between principal contestants in the contestant groups. The ratios for the principal contestants in the Transcontinental Group exceeded those for the principal contestants in the Midwestern Group by percentages which ranged from +10.3 percent to +46.3 percent in the 1946-50 period, from +15.4 percent to +54.5 percent in the 1951-56 period, and from +21.1 percent to +79.9 percent in the year 1957.

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[fol. 655] *Higher Rate of Return for Transcontinental and Eastern Groups*

The data on rate of return which relate net railway operating income after adjustment for both tax matters to net investment on the I.C.C. valuation base merit particular attention. In my judgment, these data are the most meaningful of all these measurements. On the income side, net railway operating income has been adjusted both for Federal taxes on non-transportation income and for temporary tax deferrals from rapid amortization so as to obtain the most accurate measurement, without distortions.

from these tax matters, of overall earnings from direct railroad operations. On the net investment side, the I.C.C. valuation base provides a uniform method, and, therefore, a fair method, of obtaining measurements of "value" of railroad property for comparisons on an equal basis in a divisions case.

On this basis, the rate of return for the Transcontinental Group exceeded that of the Midwestern Group by 34.2 percent in the 1951-56 period and by 37.9 percent in 1957. The rate of return for the principal contestants in the Transcontinental Group exceeded that of the principal contestants in the Midwestern Group in the 1951-56 period by 35.7 percent, in terms of the totals for the group, and by 38.1 percent, in terms of the average of individual ratios. Similarly, in the year 1957, the principal contestants in the Transcontinental Group had a rate of return which exceeded that of the principal contestants in the Midwestern Group by 39.6 percent, in terms of the totals for the groups, and

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[fol. 656] by 52.3 percent, in terms of the average of individual ratios.

On the same basis, the rate of return for the Eastern Group exceeded that of the Midwestern Group by 5.8 percent in the 1951-56 period and by 23.8 percent in the year 1957. The rate of return for the principal contestants in the Eastern Group exceeded that of the principal contestants in the Midwestern Group by 36.0 percent in the 1951-56 period and by 51.2 percent in the year 1957, in terms of the averages of the individual ratios.

Inclusion of Milwaukee Lowers Position of Midwestern Group

As noted previously, in view of the position taken by the Milwaukee with respect to the present divisions on transcontinental traffic, it would seem to be appropriate to include its figures with those of the Midwestern Group of contestants for comparative purposes. The significant margins by which the Transcontinental Group and the Eastern

Group enjoy an advantage in earning power and rate of return over the Midwestern Group are widened substantially by adding the figures for the Milwaukee to the Midwestern Group.

Considering the entire series of earning power and rate of return comparisons between contestant groups, the ratios for the Transcontinental Group exceeded those for the Midwestern Group, with the figures for the Milwaukee included, by percentages which ranged from +16.4 percent to +52.6 percent in 1946-50 period, from +21.3 percent to +65.3 percent in the 1951-56 period, and from +24.4 percent to +83.0 percent in the 1957 period. Again, the

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[fol. 657] ratios for the Midwestern Group, with the figures for the Milwaukee included, exceed those for the Eastern Group in the early post-war period. Nevertheless, in the 1951-56 period the ratios for the Eastern Group exceed those for the Midwestern Group, with the figures for the Milwaukee included, by percentages which range from +6.5 percent to +15.1 percent. The excess varied from +14.9 percent to +40.1 percent in the year 1957.

Favorable Position of Transcontinental Group Appears Even in Bearss' Groupings

The groupings of midwestern railroads used by Mr. Bearss in his Exhibits T-238 and T-275 appear most inappropriate. Nevertheless, even the in the use of these groupings, precisely as selected and constituted by Mr. Bearss, the favorable position of the Transcontinental Group is evident. In terms of the several comparisons of earning power and rate of return relating to Exhibit T-238, the ratios for the Bearss' "Midwestern Group—All Roads" exceeded those for the Bearss' "Mountain-Pacific Group" in six of eight comparisons for the period 1951-56 by percentages which range from +2.0 percent to +14.3 percent. The excess in the year 1957 is shown by percentages which ranged from +2.9 percent to +26.2 percent.

When alternate comparisons are made, moving toward appropriate and meaningful categories by taking the four Transcontinental subsidiaries and the D.M.&I.R. out of the Bearss' "Midwestern Group—All Roads" and including the Milwaukee therein, the advantage of the Transcontinental Group over the Midwestern Group in earning power and

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[fol. 658] rate of return becomes very marked. The ratios for the mountain-pacific group so constituted exceed those for the midwestern group so constituted by percentages which ranged from +14.7 percent to +49.3 percent in the period 1951-56 and from +16.3 percent to +61.2 percent in the year 1957.

When the precise selected groups designated in Exhibit T-275 as "Principal Mountain-Pacific Roads" and "Principal Midwestern Roads" are similarly compared in the 1951-56 period, the former group's percentage of excess over that of the latter group ranged from +1.5 to +19.2 in the 1951-56 period, with the single exception when the percentage was —1.6. In 1957 the former group's percentage of excess ranged from +5.1 to +38.1.

In the alternate comparisons the mountain-pacific group exceeded the midwestern in every category of earning power and rate of return and in both the 1946-50 and 1951-56 periods as well as in 1957. Taking the fourth comparison in this series, where the Bearss' "Principal Midwestern Roads" group is modified by excluding the three subsidiaries of the Transcontinental Group and by including the Milwaukee, which is then taken out of the "Principal Mountain-Pacific" group, the latter group's percentages of excess range from +21.1 to +67.4 in 1951-56 and from +19.2 to +79.9 in 1957.

Advantage in Earning Power and Rate of Return of Transcontinental Group

A clear and unmistakable conclusion flows from all these comparisons. That is the substantial advantage of the Transcontinental Group over the Midwestern Group in

terms of earning power and rate of return throughout the

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[fol. 659] entire period from 1946 through 1957. It is equally clear that by a lesser margin, in the years 1951-56 and in 1957, the Eastern Group, composed of the Official Territory lines, likewise has exceeded the Midwestern Group in terms of earning power and rate of return. Furthermore, a well defined trend toward even greater advantage is shown by these studies. These mark the continuing increase during 1951-56 and 1957 in the more advantageous earning power and rate of return position of the other two groups in relation to the Midwestern Group.

[fol. 660] BEFORE THE

INTERSTATE COMMERCE COMMISSION

Doc. No. 31503 & Sub Nos.

Exhibit No. MW 609 (JKL-2)

Witness: John K. Langum

TRANSCONTINENTAL DIVISIONS CASES

Additional Testimony of

JOHN K. LANGUM

[fol. 661]

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ADDITIONAL TESTIMONY OF JOHN K. LANGUM

In my first exhibit, numerous statistical comparisons were made of earning power and rate of return data for the three Contestant Groups of railroads in these proceedings. Similar comparisons were made as to quite different groups which have been used by witnesses for the Transcontinental railroads and for certain modifications of such groupings. Similar data were also shown by me for the principal railroads in each of the contestant groups.

In this, my second exhibit, consideration is given primarily to further aspects of the financial testimony of several witnesses for the Transcontinental Railroads, viz: Messrs. Chandler, Bearss, Edwards, Gurley, Lovett, Russell, Macfarlane, Whitman, and Boles. Here, references to groups will be in the same terms as in the first exhibit, except as otherwise indicated.

STUDIES RELATING TO THE CHANDLER EXHIBITS, T-251 AND T-252 AS SUPPLEMENTED BY THE BEARSS EXHIBIT T-276

The testimony of Mr. Marvin Chandler in previous proceedings before this Commission appears in this proceeding as Exhibits T-251 and T-252. These set forth, for the period 1949-1953, statistical studies relating to a group designated as "Eight Mountain-Pacific Railroads", the

composition of which is the same as that of Group 1, "Principal Mountain-Pacific Roads", in Mr. Bearss' Exhibit T-276. As I have already indicated, seven of these are the roads that I designate as "Principal Transcon-

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[fol. 666] tinental". For reasons already stated I do not feel that the CMStP&P can properly be included as a Mountain-Pacific road. The results of the Chandler studies are presented by textual material in Exhibit T-251 and by tables and charts (designated as "schedules") in Exhibit T-252.

Mr. Bearss, in his Exhibit T-276, produced similar schedules. He omitted the first three relating to rate of return and Schedules 25-28 relating to source and application of funds, having dealt with these subjects in greater detail in other exhibits.

Even Lower Rate of Return for Midwestern Group As Compared With Other Major Segments of American Industry

Of the remaining schedules, those numbered 4 through 17 set forth a variety of comparisons of these "Eight Mountain-Pacific Railroads" with other industries operating in the Mountain-Pacific area, viz: the electric, gas and telephone industries and several different types of manufacturing industries. The conclusion that these eight railroads "rank below other major segments of American industry" (T-251, p. 3238) certainly follows from these studies presented in Schedules 4 through 17 by Mr. Chandler and Mr. Bearss and is one scarcely to be doubted.

My own comparisons of earning power and rate of return of the Midwestern and Transcontinental Groups, however, make it clear that it may be said with even greater assurance that the Midwestern Group of roads ranks even

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[fol. 667] further below these other major segments of the nation's industry. This is because these comparisons show, as between the contestant groups, that the Midwestern Group is lower in rank than the Transcontinental Group

by a very substantial percentage in every category of earning power and rate of return. This is true when the comparisons include all Class I railroads in each group and also when only the principal railroad systems in each group are included. Even when the statistics of the Transcontinental Group are improperly diluted by inclusion of those of the comparatively low-earning CMStP&P, the modified group rank still stands higher than that of the Midwestern Group, in every instance—usually by a substantial margin.

The much lower rank of the Midwestern Group in comparison with the industries reviewed by Mr. Chandler follows as a matter of course. Accordingly, I have deemed it unnecessary to make studies setting up direct comparisons similar to those found in Schedules 4 through 17. The Midwestern Group ranks even lower in terms of rate of return as compared with other major segments of American industry than does the Transcontinental Group.

The Chandler Tests of Investor Acceptance

Beginning with Schedule 18, Mr. Chandler sets forth the results of a number of studies which he made of these eight railroads to measure or test their standing from the investor's standpoint. Under my direction, similar studies

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[fol. 668] have been made of the Midwestern Group, the Principal Contestants in the Midwestern Group (10 systems), and the Midwestern Group plus the CMStP&P. These studies also cover Chandler's Eight Mountain-Pacific Railroads, and these same eight roads minus the CMStP&P—i.e., the Principal Contestants in the Transcontinental Group (7 systems). These studies cover the 7-year period, 1949-1955, and are thus related to the same span of years shown in the Chandler schedules as extended by Bearss. In some instances these studies have been enlarged to include the years 1946 through 1957 so as to cover the entire postwar period. The results are shown frequently as averages, per annum, but in some instances, year by year statistics are also presented. Throughout these studies in respect to these exhibits of Mr. Chandler

and Mr. Bearss, my references to numbered schedules relate to their schedules of the same numbering.

Analyses of the results of these studies again show the superior position of the Transcontinental Group. This clearly appears when comparisons are made with respect to the Principal Contestants in the Transcontinental Group. Even when the CMStP&P is added to make up the group which Mr. Chandler calls the "Eight Mountain-Pacific Railroads", the same result appears with equal clarity, although the degree of superiority is slightly diminished by thus including the comparatively lower-ranking CMStP&P.

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[fol. 669] Midwestern Group Has Much More Debt and Preferred Stock In Its Capital Structure

The proportions which total debt, preferred stock and common stock and surplus constitute of total capitalization, per books, are shown in Table 3. This relates to Schedule 20. The proportion of common equity averaged 67.7 percent for the Principal Contestants in the Transcontinental Group and only 40.3 percent for the Principal Contestants in the Midwestern Group. Correspondingly, with a debt ratio of 46.3 percent and a preferred stock ratio of 13.4 percent, the Principal Contestants in the Midwestern Group had much more senior capital than those in the Transcontinental Group, where the corresponding ratios were 27.7 percent and 4.6 percent.

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[fol. 670] In Schedule 21 Mr. Chandler compared his "Eight Mountain-Pacific Railroads" with the utilities, manufacturing, and unregulated industry in terms of capital structure. In reference to the eight roads' common equity proportion of total capitalization, having in mind the earnings volatility of the railroad business, he suggests that their debt-carrying ability was much more limited than that of the electric utilities and should be closer to that of manufacturers which carry a lower portion of senior

securities in their capital structures. He stated that the "Eight Mountain-Pacific Roads" appear to him to be shouldering all the senior securities which they should or more, considering the risks of the business. If these observations are sound, they apply with even greater force to the more debt-encumbered and lower-earning Midwestern Group.

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[fol. 671] Much Greater Net Income Has Permitted Transcontinental Group to Finance Capital Expenditures With Much Less Borrowing

A Summary of Source and Application of Funds for the years 1949-1953 is shown in Table 6. The data for the "Eight Mountain-Pacific Railroads"—i.e., the seven Principal Contestants in the Transcontinental Group plus the CMStP&P—are drawn from Mr. Chandler's Schedule 26 (T-252). These data are paralleled by a similar summary for the Midwestern Group. In each instance, a column of percentages has been added to show the relation of the individual items to the totals.

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[fol. 672] Comparing these group summaries, it is noted:

For the chosen five-year period, internal sources of funds—i.e., the total of net income, depreciation, amortization and retirements—for the "Eight Mountain-Pacific Roads", $1,869,000,000, were 129 percent greater than those for the Midwestern Group, $815,000,000.

Total depreciation, amortization, and retirements for the former group, $614,000,000, was 66 percent more than that for the latter group, $370,000,000.

Net income for the former group, $1,255,000,000, was 182 percent greater than that for the latter group, $445,000,000.

Total gross additions for the "Eight Mountain-Pacific Railroads", $1,544,000,000, were 74 percent more than the total for the Midwestern Group, $885,000,000.

Funds derived from the sale of long-term debt and equipment obligations, on the other hand, totalled $403,000,000

for the "Eight Mountain-Pacific Railroads", while such debt financing aggregated $570,000,000 for the Midwestern Group. That group obtained 38 percent of its total sources of funds by such borrowing, while the former group obtained 16 percent in that manner.

Dividends paid on preferred and common stock by the "Eight Mountain-Pacific Railroads", $582,000,000, were 304 percent greater than total dividend payments by the Midwestern Group, $144,000,000.

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[fol. 673] Retained net income—i.e., net income less dividends paid—of the former group, $673,000,000, was 124 percent more than for the latter group, $301,000,000.

In considering these figures it is well to keep in mind that average net investment of the Transcontinental Group and the Midwestern Group, determined in terms of the ICC valuation base, during the same period, were $4,442,000,000 and $3,558,000,000, respectively (Exhibit MW-86, p. 2). The Transcontinental base was 25 percent greater than that of the Midwestern. On the book value base, the corresponding figures were $5,276,000,000 and $3,730,000,000. In these terms, the Transcontinental base was 41 percent greater than that of the Midwestern (Exhibit MW-86, p. 4).

It is a significant fact that the "Eight Mountain-Pacific Railroads", as against the Midwestern Group, with either 25 percent or 41 percent greater net investment in railroad plant and equipment, had dividend payments 304 percent greater, net income 182 percent greater, total internal sources of funds 129 percent greater, and retained net income 124 percent greater. These differences reflect, of course, both the greater earning power from railroad operations of the Transcontinental Group as well as that group's greater income from other sources. Total gross additions were 74 percent greater and total depreciation, amortization, and retirements were 66 percent greater.

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[fol. 674] Midwestern Group Has Made Greater Capital Outlays Relative to Net Income

Further Schedule 26 comparisons emphasize the overall difference in the standing of the Transcontinental and Midwestern groups during the five-year period. Total gross additions to plant and equipment were 123 percent of net income for the "Eight Mountain-Pacific Railroads" and 199 percent for the Midwestern Group. Total gross additions were 74 percent of total funds available from all sources except sale of long-term debt and equipment obligations for the former group and 94 percent for the latter. Funds available from sale of long-term debt and equipment obligations were only 26 percent of total gross additions to plant and equipment for the "Eight Mountain-Pacific Railroads" and 64 percent for the Midwestern Group.

These undeniable financial facts of life as regards the two groups leave no doubt that by Mr. Chandler's standard the Midwestern Group is in a much less favorable position than his group of eight railroads. As the CMStP&P is a lower earner and a heavier borrower, it is obvious that the degrees of difference in the comparisons which I am making in relation to Schedule 26 would have been widened somewhat had I recomputed this schedule for the seven other roads, that is, the Principal Contestants in the Transcontinental Group.

In summary, these group comparisons have developed beyond question the outstandingly higher measure of funds

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[fol. 675] available to the Transcontinental Group from net income. Correspondingly, the Transcontinental Group could have much less resort to debt financing. Nevertheless, the Midwestern Group spent much more on gross additions to plant and equipment in relation to net income or funds from all sources other than borrowing.

Transcontinental Group Has Important Sources of "Other Income"

Comment should be made on some of the more important sources of "other income" received by the Transcontinental Group. Such sources include very substantial operations closely associated with that Group's direct rail operations and frequently quite closely integrated with them. This includes such operations as the furnishing of refrigerator cars and icing service by the Pacific Fruit Express Company, wholly owned in equal shares by the Union Pacific and Southern Pacific Railroads. This separate corporation does for these two railroads what some other railroads, for example the Santa Fe, do for themselves by direct ownership of refrigerator cars which are used extensively in the transportation of perishable products by rail. Similar integrated service is performed by the Pullman Company in furnishing sleeping car facilities. In Mr. Bearss' Exhibit T-275, the "other income" from such refrigerator car-line and Pullman Company operations is properly included in what he terms "Funds Available from Trans-

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[fol. 676] portation Operations", although such other income is not classified as "operating income" in the Commission's Uniform System of Accounts.

In the same manner, it may be seen that such income from several other types of operation, likewise closely associated with railroad operations, might very well have been included by Mr. Bearss, such as:

> Separately incorporated motor-carrier operations, both supplementary and complementary in nature with regard to the rail operations.
>
> Pipe-line companies (primarily those owned by the Southern Pacific Company, located on the railroad right of way as a result of its policy of greater and more diversified use of its railroad property). Even the Union Pacific's large oil production is primarily derived from its railroad terminal property in the

Los Angeles Harbor area, that property being located in the very heart of the prolific Wilmington Oil Field.

Last, but not least, the income from direct rail operations of subsidiary railroad companies, wholly or in very large part owned by companies of the Transcontinental Group, might very well have been considered by Mr. Bearss as producing "Funds Available From Transportation Operations". As in the case of the car-line companies and Pullman Company, such income is produced through separate corporate ownership and operation. The character of integration with the rail operations of the parent corporations is, of course, in the nature of end-to-end extensions of rail

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[fol. 677] transportation service as distinguished from the internal integration accomplished through the car-line and Pullman companies.

So it seems that Mr. Chandler in his source and application of funds presentation was quite correct in considering funds from all sources. It would not be possible, from a financial standpoint, to divorce from these railroad companies the various subsidiary and auxiliary sources of income which are so closely associated with their direct rail operations. In fact, such subsidiary and auxiliary operations are actually a part of the over-all transportation enterprise in which each of these predominant members of the Transcontinental Group is engaged.

Expanding Midwestern Economy Brings Substantial Capital Needs for Midwestern Group

Mr. Chandler made the point that for the "Eight Mountain-Pacific Railroads" the "need for capital is a real and critical problem" for their "capital needs . . . have been great in recent years and there is every indication that such needs will continue at a substantial level in the future" (Exhibit T-251, p. 3254). Similarly, the executives of the Principal Contestants in the Transcontinental Group gave substantial emphasis to the heavy capital expenditures

needed to maintain present property and meet the demands of the expanding traffic requirements in the Mountain-Pacific Territory.

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[fol. 678] Mr. Chandler considered the prospective capital needs for the future of the "Eight Mountain-Pacific Railroads" in terms of his Schedule 26 and projections for the near future. The same reasoning applied to Schedule 26 statistics for the Midwestern Group leaves no doubt that his conclusion for these eight railroads that the "need for capital is a real and critical problem" fits the Midwestern Group with even greater certitude.

The American economy of growth and inflation in which the Transcontinental railroads operate is the same as that in which the Midwestern railroads operate. The percentage or relative economic growth in Mountain-Pacific Territory has been greater, and no doubt this will continue to be the case, than that in the Midwestern Territory. But this should not preclude consideration of the fact that the absolute amount of growth in the Midwestern Territory has generally exceeded that in the Mountain-Pacific Territory. The need for capital expenditures measured in dollars relates to the amount of growth rather than the percentage rate of growth.

The data in Tables 7, 8 and 9 relate to such comparative growth trends in terms of total population, total personal income, and total nonagricultural employment during the postwar period and earlier years. The pamphlet entitled *Long-Term Regional Trends in Manufacturing Growth: 1899-1955,* prepared and published by the United States Department of Commerce, which appears as Appendix A,

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[fol. 679] likewise presents material concerning regional growth. Thus, as is shown in Table 7, total population in Mountain-Pacific Territory grew during the period from 1946 through 1957 by 39.2 percent as compared with a rate of 18.0 percent in Midwestern Territory. Nevertheless, the postwar amount of increase in total population in terms of numbers of persons in Mountain-Pacific Territory just barely exceeded that in Midwestern Territory. Likewise,

the absolute increase in Official Territory has generally been larger than in either Midwestern or Mountain-Pacific Territory although the percentage increase has been about the same as that for Midwestern Territory.

Referring to Table 8, total personal income rose by 113 percent from 1946 through 1957 in Mountain-Pacific Territory, as compared with relative increases of somewhat over 90 percent in Midwestern Territory and in Official Territory. During the same period the dollar increase in total personal income in Midwestern Territory, even excluding Illinois, exceeded that in Mountain-Pacific Territory.

The data in Table 9 shows similar trends for total nonagricultural employment. The increase in the number of employees in nonagricultural establishments during the postwar period in Midwestern Territory, even excluding Illinois, exceeded that in Mountain-Pacific Territory, although the percentage increase was much greater in the latter territory.

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[fol. 680] Thus, as stated by the Commission in its report in Ex Parte 175, filed August 10, 1953, quoted by Mr. Chandler:

> "It is true that capital expenditures must continue to be made in large volume by the railroad companies. More or less continuous capital expenditures must constantly be made by any industry or by any company if such industry or company is to continue profitable in the face of competition of other industries or other members of its own industry."

The capital needs of the Midwestern Group of railroads have been great in recent years and they will continue at a substantial level in the future. Their inferior earning power and weaker capital structure make it even more difficult for them than for the Transcontinental Group to obtain the necessary funds to meet these capital needs. In these circumstances it is the more notable that the Midwestern Group during recent years has expended more on

capital outlays in relation to net income and has had to resort more to borrowing with their lower net income than the Trancontinental Group.

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[fol. 681]

BEARSS EXHIBIT T-275 AND RELATED COMPARISONS

In Exhibit T-275, Mr. Bearss presented a series of tables entitled "Funds Available and Funds Required, Transportation Operations". This material is closely related to the subsequent testimony of Mr. Boles, Dr. Edwards, and the five executives, viz: Mr. Lovett (U.P.), Mr. Russell (S.P.), Mr. Macfarlane (N.P.), Mr. Whitman (W.P.), and Mr. Gurley (A.T.&S.F.). A central concept in all this testimony is the so-called "percentage of funds available from transportation operations to stockholders' equity in average net investment".

Bearss' Groupings in Exhibit T-275

In the tables in Exhibit T-275 Mr. Bearss set up, for comparison, statistics for groups designated as:

"Group 1—Principal Mountain-Pacific Roads"

"Group 2—Principal Midwestern Roads"

"Group 3—Principal Official Territory Roads"

His Group 1 consisted of the seven Principal Contestants in the Transcontinental Group plus the CMStP&P. In Group 2 he included four of the Principal Contestants in the Midwestern Group, viz: Chicago and North Western; Chicago, Rock Island & Pacific; Missouri Pacific and Illinois Central. With them he grouped the two principal subsidiaries of the Southern Pacific, viz: St. Louis-Southwestern and Texas & New Orleans, together with the Chicago, Burlington & Quincy, wholly owned subsidiary of the two northern Transcontinental lines, and the Texas &

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[fol. 682] Pacific, a 78 percent owned subsidiary of the

Missouri Pacific. Of course, none of these last four named roads was a member of the Midwestern Contestant Group.

The Concept of "Balance Available for Stockholders"

The concept of "funds required", as set up in these tables, is defined to include not only the funds required for operation and the payment of fixed and contingent interest charges apportioned to transportation operations, but also all funds expended for "transportation capital expenditures", less funds derived from the issuance of new stock, bonds and equipment obligations. This latter amount is designated as "Total Funds Required for Transportation Capital Expenditures out of Railroad Operations". The amount so characterized is then dedueted from the combined total of net railway operating income (adjusted as done by Mr. Kleinsorge by adding back federal income taxes on other than transportation income), depreciation accruals, retirement charges and other reserves, to produce an amount shown in item 5, which is designated "Balance Available for Stockholders".

By this method and these designations the total amount of money which actually was available to the stockholders but which they, through their directors, chose to invest in replacement, expansion, and improvement of their properties, as capital expenditures, is treated as not having been "available" to them. Then, by relating such so-called

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[fol. 683] "available" amount to the stockholders' equity portion of the company's total net investment, per books, a very low percentage figure was obtained.

The form and method employed by Mr. Bearss in setting up the tables in his Exhibit T-275 is a novel one. Its genesis was explained by Mr. Lovett, Chairman of the Executive Committee of the Union Pacific Railroad, on page 14 of his testimony, Exhibit T-267, as follows:

> "It is generally recognized that the railroad industry as a whole has produced inadequate returns for its owners and, in this proceeding, it is a comparison of the financial performance of the various groups of

contesting roads that is important. To provide such a comparison, I asked our Accounting Department to show the financial results of railroad operations of the Union Pacific and the principal Mountain-Pacific roads and to make a comparable showing from the published records of the Midwestern and Eastern roads."

Mr. Boles, retired Director of the Commission's Bureau of Finance, stated that he participated with Mr. Bearss and others in developing the theory or method underlying these tables and that it was worked out principally between Mr. Bearss and himself (transcript of record, 3622).

After citing the respective group percentages of "Funds Available from Transportation Operations to Stockholders' Equity in Average Net Investment", shown as item 7 on page 2 of Exhibit T-275, Mr. Lovett stated this conclusion on pages 16 and 17 of his exhibit:

"The comparison thus shows that the Eastern and Midwestern roads are producing funds from railroad operations available to their stockholders at a materi-.

[fol. 684] ally greater rate than that experienced by the Union Pacific and the other Mountain-Pacific roads."

Mr. Gurley, President of the Santa Fe, undertook, on the basis of the Bearss method, to "dispel any notion that from a relative viewpoint the Santa Fe stands out ahead of our opponent groups" (T-270, p. 5). He set forth the Santa Fe's percentage of 2.13 in comparison with Bearss' eight "Principal Mountain-Pacific Roads'" percentage of 1.07 and then added individual road percentages for the CB&Q, CRI&P, IC, T&P, and StL-SW, all of which were higher than the Santa Fe. He made like comparisons with several Eastern roads. He concluded that although the Santa Fe "fared considerably better than the average of the Transcontinental Group", its "position is much less favorable when compared with the experience of our Eastern and Midwestern connections". Evidently, he meant

"financial position", for that is the expression used in comparing the Santa Fe percentage with the percentage of the New York Central, a member of the Eastern Group (T-270, p. 8).

With this same Bearss theory and method of tabulation, Mr. Macfarlane, President of the Northern Pacific, traced out the percentages, 1946 through 1955, for that railroad showing them to be considerably less than the 1.07 percent found by Bearss for the 5-year period, 1951 through 1955, and 1.05 for the 10-year period, 1946 through 1955. He pointed out that "because of the heavy demand for capital expenditures and the narrow margin of railroad revenues

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[fol. 685] over expenses, very little has remained for stockholders out of railroad operations" (T-269, pp. 9-10 and Appdx. D). His conclusion is stated thus (p. 10):

> "As shown, the low rate of return and a great demand for capital expenditures have combined to deprive the Northern Pacific's stockholders of any real return from railroad operations. For all practical purposes, the stockholders' interest in the transportation property of the Northern Pacific has been confiscated to the public use. Over the past ten years the funds available for dividends out of railroad operations have averaged only $788,000 a year, or less than 2/10ths of one percent of the stockholders' equity in the investment devoted to transportation service. Over the past five years, the balance available for stockholders has also been negligible."

Here it is noted that where Mr. Macfarlane is speaking of "funds available for dividends out of railroad operations" he obviously refers to what Bearss terms "balance available for stockholders"—item 5 in his tables.

Mr. Russell, President of the Southern Pacific, dealt with the Bearss tabulation for 1951 through 1955 by setting up a comparative tabulation for the Southern Pacific Company (Pacific Lines) which shows .32% as item 7 for that company. By way of conclusion he stated (T-266, p. 8):

> "It is demonstrated by the foregoing tabulation that, because of the common-carrier obligations of these roads to provide the facilities essential to serve this growing territory, the owners of these vast transportation properties have received substantially no return from their railroad operations."

After stressing the long-run need for new capital and the Southern Pacific's necessity to compete for its capital requirements in the nation's money markets, he pointed out

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[fol. 686] that it is at a distinct disadvantage in this respect because of its low rate of return, and it must depend on retained earnings as a primary source of funds for capital requirements. He then concluded further (pp. 8-9):

> "The unfairness to stockholders and the consequent disadvantage to the railroad properties and the communities served, by income available for the payment of dividends from railroad operations in the Mountain-Pacific group being limited to about 1% of the book value of their equity is apparent."

Mr. Whitman, President of the Western Pacific, set forth the Bearss tabulation for that railroad alone for the 10-year period 1946-1955 as showing "the degree to which the Western Pacific has devoted the funds made available from its railroad operations to the requirements of public service". He prefaced this by saying that "with respect to providing funds for capital expenditures, the Western Pacific's circumstances have been similar to the railroad industry generally in that it has had to look to the retention of earnings to finance such expenditures". The percentage of the Western Pacific which he showed for this period, .61, was referred to as evidence that "in the entire post-war period, the Western Pacific has had to devote almost all of the funds available from transportation operations to reinvestment in railroad plant to meet the growing service requirements of Mountain-Pacific territory" (T-268, pp. 10-12).

Retained Earnings Determined by Managements

This review of the executive testimony on this subject was undertaken with a view to determining what effect is

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[fol. 687] sought by these witnesses to be given to the Bearss tabulations. The Bearss method and terminology and the testimony based on it all follow the basic premise that net earnings from transportation operations (net railway operating income) are available for stockholders only to the extent that the respective railroad managements (stockholders and directors) refrain from using those earnings along with funds from other sources in payment for capital expenditures.

Now, of course, the relative amounts of net earnings to be devoted to capital expenditures and to payment of dividends are subject to managerial discretion and determination, year by year. It is obvious that the executive witnesses themselves must have had a great deal to do with establishing the policies and decisions, year by year, which determined the sums shown in the Bearss tabulations as "Balance Available for Stockholders". Such decisions at the same time determined, in part, the amounts, year by year, by which the stockholders' equity portion of average net investment was enlarged.

Retained Earnings Benefit the Stockholders

Comparisons of the Bearss sort between individual railroads or groups are of no value whatever as support for the general conclusions which these witnesses have adopted to the effect that these Mountain-Pacific roads as a group and these five of the Principal Contestants in the Transcontinental Group represented by these executives are in a

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[fol. 688] financial position inferior to the other groups of railroads with which they are compared. As we have already seen, the earning power and rates of return of these Principal Contestants in the Transcontinental Group are, in fact, on a far higher level than those of the other groups, when measured by the several methods of comparison used

in my first exhibit. Furthermore, these Principal Contestants in the Transcontinental Group are far superior to the Principal Contestants in the Midwestern Group in terms of the various tests and standards used by Mr. Chandler. Raising themselves by their own bootstraps, through the Bearss device of treating as "available for stockholders" only that part of transportation earnings which the management did not reserve for use in capital expenditures programs, and then applying this to the enlarged equity portions of investment, is not effective to support these conclusions.

The comparisons made, without reference to rates of return and other earning power statistics, and, again, without reference to funds available through income from other sources, provide no true or meaningful basis for comparison between groups or, for that matter, between individual roads, with a view to determining relative revenue needs in terms of relative financial position or credit standing.

Leaving out of consideration that part of the capital expenditures accomplished through borrowings (new money) greatly distorts comparisons when one group uses comparatively heavy borrowings for this purpose while another

[fol. 689] group, such as the Principal Contestants in the Transcontinental Group, has need to borrow comparatively little. Also, the very much greater amount of the Transcontinental Group's funds accruing from sources other than direct transportation operations but, nevertheless, closely associated therewith, is disregarded.

Furthermore, the Transcontinental Group's relatively high stockholders' portion of net investment is another distorting factor which is disregarded. Capital structure is a basic and indisputable factor in determination of rate of return on equity investment.

In this connection, it will be recalled that the group comparisons of capital structures which I made in connection with the Chandler tests showed that for the so-called "Principal Mountain-Pacific Roads" (Group 1 in Bearss' Exhibit T-275) the percentage of total debt to total capi-

talization was 28.7 percent, whereas the ratio for the Principal Contestants in the Midwestern Group was 46.3 percent, the latter being 61 percent greater than the former. The correspondingly higher ratio of common stock equity to total capitalization for Group 1 in Mr. Bearss' Exhibit T-275, in relation to the Principal Contestants in the Midwestern Group, has also been disclosed in my discussion of the Chandler tests, viz: "Eight Mountain-Pacific Roads", 65.6 percent; Principal Contestants in the Midwestern Group, 40.3 percent.

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[fol. 690] Pages 2, 3 and 4 of Exhibit T-275 relating Mr. Bearss' "Balance Available for Stockholders" to the "Stockholders' Equity Portion of Average Net Investment in Transportation Property", therefore, show relatively lower ratios of such so-called "Balance Available for Stockholders" for Mr. Bearss' eight "Principal Mountain-Pacific Roads", in part, because the seven Principal Transcontinental roads dominating that group are the ones which have built up equities for the stockholders to a far greater degree than the other groups for which comparisons are made.

So, in no reasonable sense can it be said that these tabulations present anything like a true or complete "comparison of the financial performance of the various groups of contesting roads", which Mr. Lovett said is important. Neither does it show, as Mr. Lovett stated, that Mr. Bearss' "Principal Midwestern Roads" are "producing funds from railroad operations available to their stockholders at a materially greater rate than that experienced by the Union Pacific and other Mountain-Pacific roads". Nor is there any support in these statistics for Mr. Gurley's conclusion that the Santa Fe's financial position is much less favorable when compared with the experience of its Eastern and Midwestern connections, if, as appears to be the case, that is the meaning of his testimony.

The misleading character of the Bearss tabulations, if construed and evaluated in the manner followed by these executives, is indeed well exemplified by what was said re-

garding the Santa Fe and Union Pacific Railroads. If taken

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[fol. 691] at face value, this would lead one to conclude that these two railroads, which actually are in the highest category of financial standing and credit position of any of the large railroad systems of the country, appear to be relatively poor and, in fact, inferior to the other individual railroads and groups of railroads with which comparisons were made. Actually, the very large post-war capital expenditures of the Santa Fe and the Union Pacific have been financed from net income with very little money from outside sources such as the sale of bonds, equipment obligations or stock. At the same time, their net income was such that they were able to pay substantial dividends to their stockholders and, at the same time, to benefit their stockholders, with the retained net income used in capital expenditures, by means of stock splits leading to capital gains.

The basic philosophy that capital expenditures should somehow be treated in the same category as operating expenses when evaluating the position of stockholders with respect to earnings on their investment, and that any increase in their investment, through plowed-back earnings, should be completely disregarded, is simply an erroneous interpretation of the facts of business finance and investment decision in the present-day American economy. In fact, retention of corporate earnings and their investment in plant and equipment for growth and modernization is nowadays as necessary to business enterprise as it is desirable to stockholders.

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[fol. 692] Recomputation of Percentage Shows Advantage of Transcontinental Group

The distortions inherent in the Bearss tabulations are magnified by the use of improper groupings, the deduction of acquisition adjustment accounts, and the use of net book investment instead of elements of value as the investment base. The effect of these further distortions is made ap-

parent, as between the Transcontinental and Midwestern Groups, in Table 25. Here are shown the item 7 percentages for Bearss' so-called Principal Mountain-Pacific and Midwestern Roads, and, by way of comparison, the *principal contestants* in the Transcontinental and Midwestern Groups. In each instance the percentages, computed without deduction of acquisition adjustment on both the ICC valuation base and on book value, are shown.

These recomputed percentages show that the effect of the very much greater stockholders' equity in the Transcontinental Group is more than offset by the very much lower earning power of the Midwestern Group, so that even the questionable method in T-275 fails, when principal roads in the two contesting groups are compared, to produce the result contended for by Mr. Bearss and these other witnesses. The percentages come up quite in reverse of his showing when groupings directly related to the contest in this proceeding, as between the complainant group of Midwestern roads and the defendant group of Transcontinental roads, are used. The differences are wide when the roads

TABLE 25

RECOMPUTATION OF ITEM 7, PAGE 4, EXHIBIT T-275
(10 YEAR AVERAGE 1946 - 1955)

Without Deduction of Acquisition Adjustment

	Stockholders' Equity in Net Investment	
	ICC Valuation Base	Book Value Base
Bearss' Groupings (T-275)		
Principal Mountain-Pacific Roads (Gr.1, T-275)	1.20%	1.00%
Principal Midwestern Roads (Gr.2, T-275)	2.08	2.05
Alternate Groupings		
Principal Contestants in the Transcontinental Group	1.44%	1.19%
Principal Contestants in the Midwestern Group.	1.01	.96
Principal Contestants in the Midwestern Group, plus CMStP&P	.73	.70

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[fol. 694] are thus properly grouped. The Principal Transcontinental's percentages of 1.44 and 1.19, against the Principal Midwestern's percentages of 1.01 and .96, show differentials in excess of 43% and 24%, depending on the investment base used. Shifting the CMStP&P, from the Transcontinental Group to the Midwestern Group, necessarily has the effect of widening this spread.

The Magnitude of Capital Expenditures and Their Financing

The tables in Exhibit T-275 are all predicated upon the proposition that these Transcontinental railroads should have had net income, from railroad operations alone, sufficient not only to pay their operating expenses, taxes and a fair return on their investment in railroad property, but, in addition, enough money (in addition to depreciation accruals) to cover the cost of replacement, improvement, and expansion of plant and equipment to meet the greatly enlarged volume of traffic which they have experienced in recent years. The witnesses tend to project this same proposition into the future, in which they postulate a continuation of this same high level of capital expenditures. It is asserted that this continued high demand for capital money "has created a very serious financial problem" (for Southern Pacific, see Russell, T-266, p. 5). (See also Lovett, T-267, p. 3: "the financial management of the property is alarmed"; Macfarlane, T-269, p. 15: "a very pressing problem".) In this connection, references were made to declining rates of return, notwithstanding the large capital expenditures which had been made. As indicated in the

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[fol. 695] quotations from Mr. Lovett's testimony, the impression was conveyed that the Transcontinental Group, notwithstanding its admittedly large increases in traffic volume and operating revenues in recent years, finds itself in a position inferior to the other two groups of railroads as regards the production of funds from railroad operations for further expansion and improvement and as re-

gards declining rates of return. By emphasizing their own difficulties and by referring to the comparative percentages in the T-275 tables, the definite implication is left that the Transcontinental Group will be confronted with greater difficulties than the other groups in finding the money with which to meet essential demands for expansion and improvement of plant and equipment.

In fact, during the six years, 1948-53, the Union Pacific spent $184,000,000 for new and rebuilt equipment without creating any equipment debt obligations; and in the ten years 1946-1955, with the cost of equipment purchased and rebuilt totaling more than $348,000,000, its outstanding equipment obligations were reduced from $41,273,000 to $23,192,000. During the same ten years, the Santa Fe's expenditures for new equipment acquired totaled more than $375,000,000. The only borrowings against this equipment totaled $10,855,000 in 1946-48. At the beginning of the period its total outstanding equipment obligations were $31,205,000. There were none outstanding at the end of the period.

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[fol. 696] It cannot be doubted that liberal accruals of income from sources other than direct railroad operations, combined with their direct rail income accruals, provided ample funds for these two Transcontinental companies to so largely re-equip their railroads with so little borrowing and, concurrently, to very largely rehabilitate and modernize the remainder of their railroad transportation plants, while paying liberal cash dividends to stockholders. Other railroads in this Transcontinental Group progressed along the same lines, but, generally speaking, their combined sources of funds were not as ample, and, consequently, they resorted to more borrowing. This was the situation which also confronted the Midwestern Group—and to an even greater extent.

The average principal amount of equipment obligations which the seven principal Transcontinental systems had outstanding throughout the period 1949-1955 was, in round

figures, $306,900,000. That of the complainant Midwestern Group was $384,700,000. In this connection it should be noted that the total capitalization, per books, of this Transcontinental Group averaged 80 percent greater than the Midwestern Group during the same period.

Another gauge of relative standing as regards ability to finance future equipment purchases is afforded by setting up group percentages of annual payments required on equipment obligations already outstanding in relation to total funds currently accruing from depreciation and

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[fol. 697] retirement charges against income. For such a comparison I selected the last two years for which statistics were readily available to me at the time, 1955 and 1956. The result is set forth below:

	Percentages	
	1955	*1956*
Transcontinental Group	58.35	52.86
Midwestern Group	89.64	93.60

These percentages show the proportionate parts of accruing depreciation and retirement funds which were consumed in meeting these equipment obligations in these two recent years.

It is well to have in mind in connection with these comparisons the record of relative group expenditures for these contestant groups during the period 1947-1955, inclusive, which appears in Mr. Kleinsorge's Exhibits MW-218, p. 21 and MW-448, p. 9. Taking average net investment on the elements of value basis, gross expenditures for additions and betterments for the entire period amounted to approximately 52.97 percent of average net investment for the Transcontinental Group and 49.31 percent for the Midwestern Group. On the basis of net investment, per books, percentages were: Transcontinental, 44.42 and Midwestern, 47.05. In relation to net railway operating income, adjusted to remove the distortion due to Federal taxes on

"other income", the Transcontinental Group's capital expenditures were 111 percent and the Midwestern Group's expenditures were 137 percent for the entire period.

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[fol. 698] CONCLUSION

The data included in this and my previous exhibit to my mind truly present the essential facts as to the relative earnings performance and financial position of the three railroad groups primarily involved in this case. These studies also give indications of the importance to the public of the services rendered by the respective railroad groups. In this I take it there can be no doubt that each of these groups is of great public importance. Certainly from the public standpoint the Midwestern Group is of no less importance than the other two groups.

In earning power and rate of return from direct railroad operations the Transcontinental Group stands far out ahead of the Midwestern Group. The Transcontinental Group's position as to credit rating and favor among investors is therefore much higher than that of the Midwestern

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[fol. 699] Group. These attributes are enhanced by the relatively larger amount of income enjoyed by the majority of the principal Transcontinental roads from separately incorporated subsidiary transportation operations and additional items classed as non-operating income. It is clear, however, that, in terms alone of the data for direct railroad operations, the earnings performance and financial position of the Transcontinental Group is strikingly higher than that of the Midwestern Group.

To a considerably lesser degree the Eastern Group's standing is also shown to have been higher than that of the Midwestern Group since 1950, it having been in a moderately lower position in the 1946-1950 period. The Eastern Group forged ahead in the later years and stood in a con-

siderably better position than the Midwestern Group in the subsequent 6-year period and in 1957.

Measured by the various tests employed on behalf of the Transcontinental Group by Mr. Chandler, that group again stands out very definitely ahead of the Midwestern Group. The application of these measurements to the representative principal roads in each of these contestant groups demonstrated the much higher credit standing and greater financial security of the Transcontinental Group in every instance. This was even apparent when Mr. Chandler's own group of so-called "Eight Mountain-Pacific Roads", which included the Milwaukee, was used. The high in-

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[fol. 700] vestment stature of key members of the Transcontinental Group is manifest from their dominance in railroad common stock holdings of all groups of leading institutional investors.

In applying Mr. Chandler's sources and application of funds test to the Principal Midwestern Contestants it was found that a very much higher percentage of net income and of funds available from all sources, including borrowed funds, was expended in making gross additions to plant and equipment of the Midwestern Group than of the Transcontinental Group. This was true notwithstanding the very extensive improvement programs completed by the Transcontinental roads in the post-war years. The "need for capital" of the so-called "Eight Mountain-Pacific Railroads" emphasized by Mr. Chandler is shown to have been exceeded significantly by the needs of the Midwestern Group. While the former group's gross amount spent for additions and betterments during the 1949-1953 period was 74 percent greater than the amount so spent by the Midwestern Group, the Transcontinental Group's percentage relationship to net income was 123 percent against 199 percent for the Midwestern Group.

Obviously, and quite naturally, there is a considerable variation in earning power among the different individual

railroads in each group. This should be noted, but unless a different basis of divisions is to be prescribed as between individual carriers, which I understand is not contemplated or asked for by any of the participants here, it appears

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[fol. 701] to me that the primary consideration should be given to the comparisons in terms of the group figures, without modification or distinction in relation to the various high or low earners in the several groups. Hence, I have given no effect to the suggestion made by Mr. Boles and some of the Transcontinental railroad presidents that low earners in the Eastern and Midwestern Groups be eliminated therefrom for statistical purposes.

Considering earnings from direct railroad operations alone, the relatively much lower earnings of the Midwestern Group have left it in a position where it has fallen short of earning a fair return after payment of operating expenses and taxes to a greater extent than either of the other groups; and this is particularly true in comparison with the Transcontinental Group where the disparity is of large proportion. Furthermore, the continued trend has been toward greater improvement in earning power and financial condition in the other two groups in relation to the Midwestern Group.

From my studies it is apparent that the Midwestern Group is in far greater need for additional revenue than the Transcontinental Group and moderately so in comparison with the Eastern Group.

[fol. 702]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

WASHINGTON, D. C.

I.C.C. Docket 31503 and Sub Nos.

Exhibit T-632 (FKE-6)

Witness: Ford K. Edwards

TRANSCONTINENTAL DIVISIONS CASES

Statement of Ford K. Edwards in Response to Criticisms of Mountain-Pacific Lines' Cost Study, Made by the Eastern and Midwestern Lines, Together with Results of the Cost Study Corrected and Revised in Light of Those Criticisms.

[fol. 703] The following tables, in the same form as the table presented above for Official territory, compare the results of our initial tabulation of car miles of way train service per car in transcontinental traffic with the revised tracing of the Midwest. Both figures are compared with the amount of way train service built into the application of transcontinental traffic of Rail Form A line-haul costs embracing system average way train service:

Car Miles per Car in Midwestern Territory:

1. Official Transcontinental Traffic (average haul 1,046 actual miles):

Implicit in Rail Form A unadjusted (8.08% of total car miles)	84.5 miles
As traced in my Exhibit T-314	0 8 miles
As re-traced in light of Witness Carpenter's working papers for equivalent of bridge line-haul service	1.0 miles

2. Midwest-Transcontinental Traffic (average haul 978 actual miles):

Implicit in Rail Form A unadjusted (8.08% of total car miles)	79.0 miles
As traced in my Exhibit T-314	9.3 miles
As re-traced in light of Witness Carpenter's working papers	10.1 miles

Car Miles per Car in Mountain-Pacific Territory:

1. Official-Transcontinental Traffic (average haul 1,213 actual miles):

Implicit in Rail Form A unadjusted (4.81% of total car miles)	58.3 miles
As traced in my Exhibit T-314	34.3 miles
As shown in my revised study*	33.0 miles

2. Midwest-Transcontinental Traffic (average haul 1,272 actual miles):

Implicit in Rail Form A unadjusted (4.81% of total car miles)	61.2 miles
As traced in my Exhibit T-314	34.1 miles
As shown in my revised study*	30.6 miles

* The minor changes reflected in my revised study are due largely to the changes in definition of traffic included in the sample, made to minimize controversy with the Midwest and East.

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[fol. 704] As shown, use of Midwestern system average line-haul costs assumes 84 and 79 miles of way train service (a weighted average of 82 miles), whereas only 1 and 10 miles (a weighted average of 4.6 miles) of the costly way train service is performed on transcontinental traffic. In Mountain-Pacific territory, the system average imputes more way train service than is performed on transconti-

nental traffic but in far, far less degree than for the Midwest and, as shown previously, for the East.

Summing up the relationships of way train haul in transcontinental traffic as compared with the territorial average in the respective territories, we find the following relationships:

Way Train Miles per car for Transcontinental Haul

	As Experienced on Transcontinental Traffic (1)	As Reflected in Territorial Average Train for Same Haul (2)	Percent Column (1) of Column (2) (3)
Official	9.0 miles	42.0 miles	21.4%
Midwest—			
On Official Traffic	1.0 miles	84.5 miles	1.2%
On Midwest Traffic	10.1 miles	79.0 miles	12.8%
Weighted Average	4.6 miles	82.3 miles	5.6%
Mountain-Pacific—			
On Official Traffic	33.0 miles	58.3 miles	56.6%
On Midwest Traffic	30.6 miles	61.2 miles	50.0%
Weighted Average	32.0 miles	59.5 miles	53.8%

My review and retracing of the facts underlying my cost study provide further proof of the very great need for adjustment of Rail Form A costs as applied to the transcontinental traffic where cost characteristics differ so markedly, and in such varying degrees, from system average traffic in the three territories.

[fol. 705] The cost results shown in Exhibit T-314, and Appendices C and D herein, compare revenues and costs of railroad groups. Cost-revenue comparisons by territories cannot be made because the present divisions do not in all cases break the revenue at the territorial borders. However, the costs have been prepared separately by territories and the cost comparisons by territories were described in my oral direct testimony at the February 4, 1957, hearing (Tr. pp. 3511-3519). The unit costs of handling transcontinental traffic were summarized in my Exhibits T-316 and T-317 and cost scales in the same form, constructed from the working papers underlying Appendix C, are set forth in Appendix E hereto.

The revised cost scales show that, at 600 miles, the approximate average haul of this traffic in the East, the cost of handling transcontinental traffic in the East is 33.10¢ per cwt. as compared with a cost of 40.04¢ per cwt., or 21.0% higher, for a like haul in Mountain-Pacific territory. At 1,000 miles, the approximate average haul in the Midwest on Midwest-Mountain-Pacific traffic, the Midwest cost of handling transcontinental traffic is 39.04¢ per cwt., as compared with a cost of 52.59¢ per cwt., or 34.7% higher, for a like haul in Mountain-Pacific territory. Cost scales are also shown for the Midwestern lines' bridge haul traffic between Official and Mountain-Pacific territories.

* * * * * * *

balance at through train cost of .0554d per mile.

Appendix E, FKE-6
Page 1 of 3
(Does not include Canadian and Mexican traffic.)

Comparison of Terminal and Line-Haul Costs Incurred in Handling Transcontinental Traffic
1956 Unit Costs

Line No.	Item	Traffic Between Official and Mountain-Pacific 1/			Traffic Between Midwest and Mountain-Pacific 2/	
		Mountain-Pacific Territory (a)	Midwest Territory (b)	Official Territory (c)	Mountain-Pacific Territory (d)	Midwest Territory (e)
	Terminal					
1.	Terminal costs - dollars	1,030,494	8,784	621,007	808,456	558,206
2.	Hundredweight	10,820,500			10,109,240	
3.	Cost per cwt. - cents	9.52		5.74	8.00	5.52
	Line-Haul - Way Train					
4.	Way train costs - dollars	401,379	6,866	64,584	309,002	54,988
5.	Hundredweight-miles (thousands)	414,735	11,884	111,051	348,648	121,893
6.	Cost per cwt.-mile-cents	.0968	.0578	.0582	.0886	.0451
	Line-Haul - Thru Trains					
7.	Thru train costs - dollars	5,867,070	3,976,897	2,937,112	5,347,681	3,232,624
8.	Hundredweight-miles (thousands)	12,162,358	11,280,464	6,468,538	12,381,168	9,687,601
9.	Cost per cwt.-mile-cents	.0482	.0353	.0454	.0432	.0334

1/ Average load: 487 cwt. per car
2/ Average load: 516 cwt. per car

Costs in Cents Per Hundredweight Incurred in Handling Transcontinental Traffic Year 1956

Miles	Traffic Between Official and Mountain-Pacific			Traffic Between Midwest and Mountain-Pacific	
	Mt.Pac. Territory (a)	Midwest Territory (b)	Official Territory (c)	Mt. Pac. Territory (d)	Midwest Territory (e)
100	15.94	3.55	10.40	13.71	8.98
200	20.76	7.08	14.94	18.03	12.32
300	25.58	10.61	19.48	22.35	15.66
400	30.40	14.14	24.02	26.67	19.00
500	35.22	17.67	28.56	30.99	22.34
600	40.04	21.20	33.10	35.31	25.68
700	44.86	24.73	37.64	39.63	29.02
800	49.68	28.26	42.18	43.95	32.36
900	54.50	31.79	46.72	48.27	35.70
1000	59.32	35.32	51.26	52.59	39.04
1100	64.14	38.85	55.80	56.91	42.38
1200	68.96	42.38	60.34	61.23	45.72
1300	73.78	45.91	64.88	65.55	49.06
1400	78.60	49.44	69.42	69.87	52.40
1500	83.42	52.97	73.96	74.19	55.74
1600	88.24	56.50	78.50	78.51	59.08
1700	93.06	60.03	83.04	82.83	62.42

[fol. 707]

1800	97.88	63.56	87.58	87.15	65.76
1900	102.70	67.09	92.12	91.47	69.10
2000	107.52	70.62	96.66	95.79	72.44

Sources:

Col. (a): 9.52¢ Terminal, 33.0 miles way train @ .0968¢ per mile, balance at through train cost of .0482¢ per mile.

Col. (b): 1 mile way train @ .0578¢ per mile, balance at through cost of .0353¢ per mile.

Col. (c): 5.74¢ Terminal, 9.0 miles way train @ .0582¢ per mile, balance at through train cost of .0454¢ per mile.

Col. (d): 8.00¢ Terminal, 30.6 miles way train @ .0886¢ per mile, balance at through train cost of .0432¢ per mile.

Col. (e): 5.52¢ Terminal, 10.2 miles way train @ .0451¢ per mile, balance at through train cost of .0334¢ per mile.

[fol. 709]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

I.C.C. Exhibit No. 31503 and Sub. Nos.

Exhibit T-648 (AJS-7)

Witness: A. J. Stilling

Transcontinental Divisions Cases

Divisional Integer Scales

Presented in Answer to

Witness L. E. Butler (Exhibits E-312 and E-487)

[fol. 710] I am the same A. J. Stilling who previously testified in these proceedings.

In our Exhibits T-299 through T-305, Witness Parr and I set forth the reasons why divisional integer scales reflecting rate scale progressions would be grossly unfair to the long haul carriers of transcontinental traffic. It was our basic conclusion that integer scales for application to the transcontinental traffic must reflect the progression of cost scales. The integers must also reflect differences in relative costs of handling transcontinental traffic, differences in revenue needs from that traffic and any other factors that may affect just and reasonable divisions.

In Exhibit E-487, Witness L. E. Butler has stated his agreement with our basic conclusion (page 1):

> "Based upon many years of experience in divisions matters I am of the opinion that relative costs of service here afford the fairest common standard by which to weigh the relative contribution of the participating groups of carriers in the performance of the joint transportation."

Mr. Butler has implied in Exhibit E-487 (LEB 75) page 10, that Witness Parr and I had advocated use of "assumed equal costs" in contrast with "an ascertained relative cost basis." This does not correctly state our testimony. It is a fundamental of our position and I strongly emphasized that "differences in the amount and cost of service" must be taken into account and stated that other witnesses would deal with the higher costs in Mountain-Pacific territory. (Exhibit T-302, pages 2, 22-23). Witness Parr also emphasized the necessity of acting "to give effect to differences [fol. 711] as between the respective territories and groups of carriers . . . . Differences in the cost of handling the transcontinental traffic, under efficient management and operations." (Exhibit T-299, page 24). This should make it plain that we agree with Mr. Butler in the principle that the cost scales should reflect ascertained differences in costs. Our position is that the costs should be based on an ascertainment of the cost of handling the transcontinental traffic in issue in these proceedings, and it may not be assumed that costs are equal or that the costs of handling average traffic represent the cost of handling transcontinental traffic.

As a traffic officer with experience in the field of railroad freight rates and divisions I am not qualified to testify as to what are the relative costs of transporting transcontinental traffic and I feel sure that Witness Butler, also, considers himself unqualified to testify about costs in his territory. Our group relies upon the results of the cost study introduced by Witness Ford K. Edwards.

Witness Butler explains the Heywood costs as follows (Exhibit E-487, p. 13):

> "This scale of relative costs is illustrative only, and I am not to be understood as testifying that these are necessarily the costs which the Eastern lines will ultimately urge as the most significant for Commission consideration. These scales of relative costs illustrate how the Eastern lines would like to have the Commis-

sion proceed in arriving at fair scales of divisional factors."

My view on the procedures to be employed if divisional integer scales are used, directly or indirectly, in making

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[fol. 712] transcontinental divisions may be summarized as follows:

1. Obtain unit costs measuring the actual costs of handling Official-transcontinental and Midwest-transcontinental traffic in each of the respective territories.
2. Develop the ratio of actual to short-line miles in handling transcontinental traffic in the respective territories to convert the line-haul unit costs to a short-line basis.
3. Construct from the unit costs, scales in 50 mile blocks, using the mileage at the midpoint of each block.
4. Adjust the scales to reflect relative revenue needs from the transcontinental traffic.

No minimum should be provided since, by definition, a proper cost basis would reflect the services rendered in each mileage block.

I do not understand Mr. Butler's testimony as differing with my position as to the basic principles to be employed in constructing integer scales (paragraphs 1 and 2 above). In respect to paragraph 4, I understand that, knowing the great dependence of the Mountain-Pacific railroads on the transcontinental traffic and the minor proportion of the Eastern lines' revenues derived from that traffic, Witness Butler's position is that the relative importance of this traffic to the revenue needs of the carriers "Should Have No Weight" (Exhibit E-487, page 21).

Midpoint of Mileage Blocks

Mr. Butler disagrees with the conclusion stated in my prior testimony on the technical problems of the midpoint

of the mileage block and the use of a minimum. In reply

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[fol. 713] to Mr. Butler's answer on the mileage block problem, it is apparent from his own showing that application of the 25.5 miles midpoint produces fair divisions for the Eastern lines. Page 1 of Appendix D of Exhibit E-487, shows an average haul in the 1-50 mile block out of Chicago of 35 miles to the stations selected by Witness Butler, 15 miles short of the end of the 50 mile block. Page 3 of the same Appendix shows an average haul in the 1-50 mile block out of E. St. Louis of 19 miles, or 31 miles short of the 50 mile block. Mr. Butler thus seeks a bonus payment for 15 miles and 31 miles of service not performed. Taken as a whole, Mr. Butler's examples also show properly offsetting variations above and below the midpoint. Thus, on the basis of Witness Butler's own exhibit, based on stations of his own selection and not as a representative sampling of all of the traffic, it shows that use of the midpoint of the mileage blocks is proper and that use of the end of the mileage blocks gives the East an unfair and improper allowance for mileage not actually performed.

The ultimate in refinement, and also in complexity, would be to calculate average hauls to each 50 mile block via each gateway. Use of the midpoint is the substantial equivalent of this process. Witness Butler's alternative is to use the extreme end of the mileage block. This is almost always wrong and is always wrong in the same direction. Such an arbitrary addition of mileage creates an unfair distribution of revenue for the benefit of the short haul roads, as explained in my Exhibit T-302, page 21 and Appendix F.

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[fol. 714] Minimum Divisions Provisions

Witness Butler also advocates a 15% minimum in conjunction with cost scale integers. A minimum provision is entirely inconsistent with a cost basis of integers for the reasons set forth in my Exhibit T-304. A proper minimum

is built into the cost scale with its allowance for terminal and related costs and the use of a minimum which produces a division different from that produced by the cost scales is necessarily wrong by the amount of the difference.

Witness Butler relies on the circumstances of very short haul carriers in support of a minimum. But these circumstances simply reflect deficiencies in Witness Heywood's system average cost scales, and do not provide any basis for a minimum. The system average cost scales spread over all miles the local service and interchange costs incurred by a very short haul carrier in the first mileage block. Witness Butler would compensate for this deficiency by a minimum provision, but would also leave the costs in the average for the benefit of the longer hauls in the East. This is a clear example of double counting.

The proper approach is to separate local (way train) and through service and include the local service in the first mileage block. A further refinement is to separate one interchange from the line haul costs for each car, and include that interchange allowance in the first mileage block. In his Exhibit T-FKE 10 App. L, Dr. Edwards has set forth the

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[fol. 715] basis for such a refinement in the costs for Official territory. No comparable adjustment is needed in the Midwest or Mountain-Pacific territories since the interchanges incurred on transcontinental traffic are spread over greater distances and only an insignificant volume of traffic falls in the very low mileage blocks.

If the first mileage block includes not only a terminal cost, but also the higher cost of local service and an interchange cost, the relative services of a very short haul carrier are protected. This builds into the divisional integers themselves an automatic minimum property reflecting the services of the short haul lines. If the relative cost of such a short haul carrier, when taken with the cost of a 2,000 mile haul in the West, produces 5% of the total revenue, then this is a fair division under Witness Butler's own statement of relative costs.

Witness Butler's comment that "In no other interterritorial divisional arrangement that I know of does one group of roads receive as little as 5 per cent of the total revenue" (Exhibit E-487, page 29), simply reflects the fact that on no traffic other than transcontinental traffic are there ever hauls of over 2,000 miles contrasted with hauls of less than 50 miles. The Missouri-Illinois, a road whose haul on transcontinental traffic is always very short, has been receiving for a generation less than 4½% of the total revenue for an average haul of about 60 miles (Exhibit T-304, table facing page 10). Until other roads brought this divisions proceedings, no complaint was ever made against these divisions by

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[fol. 716] the Missouri-Illinois because it believed its portion of the revenue to be at least commensurate with its share of the service.

The Emphasis on Short Haul Eastern Roads

Witness Butler emphasizes the reduction that other short haul Eastern carriers would receive under a cost scale. (Exhibit E-487, page 34 and Appendix D.) With adjustment for interchange service, the reduction would be somewhat less. But the important reason for the reduction is Witness Butler's own proposal for integers applied to 50 mile groups. In contrast, the present divisions reflect broad groupings. For example, one group covers large portions of Indiana, Michigan and Ohio, and the short haul points receive the same 13% division as the much longer hauls within that group. Witness Butler's proposed 50-mile block would break the present grouping into much smaller groups. Other things being equal, that change alone reduces the divisions for the shorter Indiana hauls and increases the divisions at the longer Ohio hauls within the present single group. Citing the reductions at the shorter hauls, Witness Butler seeks to resist those reductions with a minimum provision while retaining for the longer hauls divisions based on their distance from the gateways. This is another illustration of attempting to have it both ways, and the

double counting inherent in the proposal for a minimum division.

Witness Butler also cites revenues to short haul Eastern lines on particular cars of transcontinental traffic, without ever relating such revenues to the costs of the short haul

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[fol. 717] carrier and the relative cost of its connections to the Pacific Coast. Many of the illustrations of low revenues are due to the low level of revenues for the total haul, a problem that must be solved through rate action, not divisions. This is especially true of Appendix G of Exhibit E-487, where the showing is confined to fresh fruits and vegetables.

The Effort to Obtain a Two-Way Initial Break Over Eastern Points of Interchange

In view of the three-way contest in these proceedings, the logical way to meet the issues is to develop costs and construct scales separately for Mountain-Pacific, Midwestern and Official territories. With proper costs for each territory and divisions which reflect those costs, differences in breaking points would not affect the distribution of revenue, as shown in my Exhibit T-303, and as also indicated by Witness Heywood's Exhibit E-504, page 26. In view of this fact, the Eastern lines' advocacy of a two-way break over gateways with the Eastern lines must represent an effort to obtain an unwarranted benefit in the hope that integers reflecting a rate scale progression are prescribed.

Of course, if, but only if, the divisional scales are constructed on actual costs, no line or group of lines would be prejudiced by an initial two-way break over Eastern gateways. With such a break, a scale would have to be constructed for the entire Western haul with the appropriate circuity factor, and separate scales then constructed for sub-

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[fol. 718] dividing the Western revenue on the same traffic as between the contesting Midwestern and Mountain-Pacific roads, all of which would unnecessarily complicate the disposition of the three-way controversy over divisions on the

same traffic. Moreover, as stated, if done on that basis, the Eastern lines lose all interest in a two-way break.

The Standards Set Forth by Witness Butler in Exhibit E-312

Integer scales constructed in accordance with the procedures which I have outlined above would meet each of the standards set forth by the Eastern lines in their criticism of the Midwestern lines' proposal. In Exhibit E-312, Witness L. E. Butler listed the following criticisms:

> "First it [the Midwestern lines' proposal] inflates the short line mileages in the West. Second, through use of 50-mile block factors between each two primary break points on a route, the proposal allows Western lines compensation for mileage service not performed. Third, by reason of the construction of conventional divisional scales,* the multiple application of such factors in the West serves improperly to inflate the total factor west. Fourth, observance of a 15 per cent minimum between multiple primary break points operates further to increase the total Western factor." (pp. 5-6)

These standards set forth by Mr. Butler are fully satisfied by my suggestions as to the proper construction of divisional integer scales.

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[fol. 719] First: The divisional integer scales constructed as I have suggested would contain no inflation of short line mileage. The unit costs should be based on actual miles over the routes-of-movement of the transcontinental traffic, and such cost data should be adjusted for application to short line distances through the use of circuity ratios which measure the relationship of actual to short line miles developed from the transcontinental traffic as it moves in each of the respective territories.

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* By this, Witness Butler means scales "based on the Docket 28300, Appendix 10 first-class rates" (Exhibit E-312, pp. 7-8).

Second: The effect of the 50-mile blocks is eliminated by application of the scales at the midpoint of each block.

Third: The rate scale progression has no influence on the scales constructed directly from cost scales.

Fourth: No minima are applied, since allowances for terminal services, including interchange services, are built into the scales themselves.

In his Exhibit E-312, Witness Butler also made the following general comment on the Midwestern lines' proposal:

> "The use of multiple break points in the west only would require different scales of divisional factors for the respective groups of carriers which would take that fact into account. Otherwise, they would fail to reflect the relative costs of the services performed by the several carrier groups. Such separate scales should include no terminal factor for an intermediate carrier group. (p. 19)

The divisional scales constructed as I have suggested would satisfy each of these standards as well: The scales would be different for each of the territorial groups; no terminal

[fol. 720] factor is included for intermediate service; and the scales are based on and, therefore, "reflect the relative costs of the service performed by the several territorial groups," as urged by Witness Butler.

Accordingly, each of the standards of divisional integer construction set forth by Witness Butler in his Exhibit E-312 are satisfied by the integer scales constructed in the manner which I have described.

Mr. Butler made one further comment immediately following the statement from Exhibit E-312 quoted above:

> "But such a system of divisional factors would still retain the undesirable characteristic of fixing different divisions for identical service in the East, out of a given rate, depending upon the route in the west." (p. 19)

Mr. Butler has repeated this observation in his Exhibit E-487, pages 7-9. This is a curious position since different divisions for identical service within the East are inherent in any application of integers to three or more territorial groups (such as in the case of Official-Southwestern traffic moving on routes through the South as prescribed in Docket 29886). Mr. Butler's desire for equalization of divisions over different routes can be met by the parties agreeing to the use of divisional integers to obtain equalized group per cents, based on the weighted average movement to each divisions group.

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[fol. 721]

BEFORE THE
INTERSTATE COMMERCE COMMISSION

I.C.C. Docket 31503 and Sub. Nos.
Exhibit T-652 (HJB-9)
Witness: H. J. Bearss

RATE OF RETURN COMPARISONS
In Response To
Exhibits MW-608 and MW-609—Witness John K. Langum

Appendix A
Page 2 of 3 Pages

BASES FOR RATES OF RETURN

1955 through 1957

Items	1955	1956	1957
MOUNTAIN-PACIFIC GROUP 3/			
Net Railway Operating Income			
Per Books	$ 263 279 200	$ 244 835 927	$ 228 457 319
Per Books, Normalized	211 963 812	194 378 056	180 496 649
Including Both Tax Adjustments	230 604 380	214 373 949	202 430 921
Schedule 211N, Investment Basis 1/			
Before Acquisition Adjustment	6 737 738 933	6 885 133 991	7 034 444 339
After Acquisition Adjustment	6 499 527 903	6 641 474 043	6 786 828 226
ICC Elements of Value Basis 2/			
Before Acquisition Adjustment	5 742 600 233	5 883 297 815	6 101 592 384
After Acquisition Adjustment	5 504 389 203	5 639 637 866	5 853 976 269
ICC Elements of Value Basis - End of 1957 and Changed for Time Lag 4/			
Before Acquisition Adjustment			6 303 354 377
After Acquisition Adjustment			6 057 474 598
OFFICIAL TERRITORY 5/			
Net Railway Operating Income			
Per Books	$ 481 454 332	$ 466 718 173	$ 385 277 842
Per Books, Normalized	413 736 228	400 541 754	337 531 866
Including Both Tax Adjustments	423 436 911	413 097 411	346 594 646
Schedule 211N, Investment Basis 1/			
Before Acquisition Adjustment	11 491 684 679	11 524 569 140	11 699 183 886
After Acquisition Adjustment	11 443 820 286	11 480 402 908	11 621 863 688
ICC Elements of Value Basis 2/			
Before Acquisition Adjustment	11 067 485 332	11 137 898 583	11 388 984 948
After Acquisition Adjustment	11 019 723 587	11 093 732 347	11 261 664 741
ICC Elements of Value Basis - End of 1957			
Before Acquisition Adjustment			11 452 161 142
After Acquisition Adjustment			11 374 614 157

[fol. 723]

BEFORE THE
INTERSTATE COMMERCE COMMISSION

I.C.C. Docket 31503 and Sub. Nos.

Exhibit T-653 (HJB-10)

Witness: H. J. Bearss

Rates of Return, Weighted by Relative Participation in Transcontinental Traffic

In Response To

Exhibit E-501—Witness J. L. Heywood

Exhibits MW-608 and MW-609—Witness John K. Langum

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[fol. 724] Every computation of a group rate of return involves some form of weighting to get an average for the group. The issue as to what constitutes a proper weighting cannot be side-stepped. As noted in my Exhibit T-274, relating the aggregate net railway operating income for a group of roads to the aggregate investment constitutes a weighting on the basis of the size of the roads. Such a weighting is appropriate when the whole of every railroad's operations is involved, as in an Ex Parte case when a general revenue increase is sought by raising all or a very large proportion of all rates. It is not proper to borrow that procedure from an Ex Parte case and apply it in a divisions case when the relative participation of the lines within the group in transcontinental traffic varies materially from their proportion of the group's investment.

Rate of return data is of interest in appraising the financial need of the different groups of roads. An order in a

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[fol. 725] divisions case can affect the financial fortunes of the roads involved only to the extent that traffic involved in the proceeding travels over the roads in each group. In a transcontinental divisions case, the proper method of weighting rates of return is on some basis that measures

each line's participation in that traffic. Otherwise, revenues may be transferred from one group to another because of the size of certain individual carriers and the consequent weight attached to their low rate of return, when in fact they have only a minimal participation in transcontinental traffic in comparison with the proportion handled by other carriers within the same group. A simple example that highlights the problem may be helpful.

				Weighted on Investment		Weighted on Traffic Participation	
	NROI (1)	Net Investment (2)	Rate of Return (3)	Percent of Total (4)	Weighted Rates of Return (5)	Percent of Total (6)	Weighted Rates of Return (7)
Road 1	$8	$400	2.0%	80%	1.6	20%	.4
Road 2	$4	$100	4.0%	20%	.8	80%	3.2
				100%	2.4	100%	3.6

One method of obtaining an average rate of return for these two roads is to take a simple average of 2.0% and 4.0%, which is 3.0%. This method fails to take any account of the relative size or importance of the two roads. This simple average method was used by Witness Langum in his Exhibit MW-608 and was properly criticized by the eastern lines as not taking into account the size of invest-

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[fol. 726] ment or importance of transcontinental traffic to the individual roads.

The method of obtaining average rates of return commonly employed in general rate cases is to aggregate the net railway operating income ($8 plus $4 equals $12) and divide by the aggregate net investment ($400 plus $100 equals $500). This produces an average rate of return of 2.4%. As shown in columns 4 and 5 of the table above, this use of the aggregate data is the same, as a matter of arithmetic, as weighting the individual rates of return by the investment of each road.

If Road 2 in the above example handled none of the traffic involved in a divisions case, however, it is perfectly apparent that the rate of return to be considered for the group must give no weight to the rate of return of Road 2. That road would have no interest in the divisions under consideration, its experience would have no bearing upon the issue and no transfer of divisions to or from the territory in which Road 2 operates could affect the rate of return of Road 2 if it did not participate in the traffic. The same principle applies, differing only in degree, whenever the relative participation in the traffic by a road differs from the relative size of its net investment to the net investment for the group as a whole. Columns 6 and 7 of the table above show the difference in weighted rates of return when the individual rates of return are weighted by the roads' participation in the traffic instead of by the size of their net investment. When weighted on the basis of investment, the group rate of return is 2.4 per cent. If we assume that the proportionate participation in the traffic for these

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[fol. 727] two roads is just the reverse of their respective proportions of the total investment, we find that the weighted rate of return for the group jumps up to 3.6 per cent. A showing of group rates of return solely on the basis of a weighting in accordance with the size of individual road investments does not measure the relative financial needs of the different groups of roads as related to the transcontinental traffic.

Witness Langum devotes some 24 pages of his Exhibit MW-608 to a discussion of "Earning Power and Rate of Return Comparisons in Terms of Averages of Individual Ratios." He states that "These comparisons in effect weight the individual roads equally as individual enterprises making up the contestant groups." (p. 73). Witness Heywood has reproduced some of these ratios in his Exhibit E-611A. As a comparison of the simple average of 3.0% with the weighted results shown in columns 5 and 7 of the table

on page 2 hereof indicates, these averages of individual ratios completely miss the mark in that they fail in any significant way to show the relative financial needs of the different groups of roads. When the rate of return of the Minneapolis, St. Paul & Sault Ste. Marie RR. System, with 5.66 per cent of the net investment of the group of ten principal midwestern systems as used by Witness Langum and only 2.54 per cent of the group's transcontinental ton-miles, is given equal weight with the Rock Island, having 14.21 per cent of the net investment and 29.23 per cent of the transcontinental ton-miles, it is evident that the average result for the group will have lost all meaning.

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[fol. 728] The effect of the Territorial Method is to weight the rate of return for the split roads in the group rate of return for each territory to the extent of their transcontinental traffic participation in each territory. This basis meets the split road problem. It appears to solve a problem that suggested itself to the Examiner when, in commenting on my Exhibit T-275, he called attention to the fact that "The Chicago, Milwaukee, St. Paul & Pacific Railroad Company was named as one of 8 roads in group 1 (Principal Mountain-Pacific Roads) but was not included in either of the others (Principal Midwestern Roads and Principal Of-

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[fol. 729] ficial Territory Roads)." As Appendix C indicates, the Examiner went on to request available information on that part of CMStP&P's traffic that was handled in Mountain-Pacific territory.

The Territorial Method resolves the problem faced by Witness Langum in his MW-608 with respect to the Milwaukee, for its rate of return will influence the group rates of return of the three territories to the extent that its transcontinental traffic takes place in each territory. Furthermore, it may be noted that the Santa Fe was placed in groups on both sides of the gateways in the Appendix to the Commission's report in Docket 15234 (203 I.C.C. 354-5).

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Table 6
Weighted Rate of Return Comparisons
Using
Net Railway Operating Income - Including Both Tax Adjustments
I.C.C. Schedule 211N - Average Net Investment and Acquisition Adjustment
1955 through 1957

Groups	1955	1956 Weighted On		1957	
	Property Base As Above	Transcontinental Ton-Miles - Territorial Method*	Property Base As Above	Transcontinental Ton-Miles - Territorial Method*	Property Base As Above	Transcontinental Ton-Miles - Territorial Method*
			Rates of Return			
1. Midwestern Group - all roads, excluding C&NW and CStPM&O	4.09	3.87	3.89	3.72	3.28	3.18
2. Midwestern Group - all roads	3.82	3.73	3.49	3.46	3.04	3.05
3. Mountain-Pacific Group	3.55	3.69	3.23	3.35	2.98	3.18
4. Official Territory	3.70	3.71	3.60	3.29	2.98	2.43
5. Official Territory, excluding NYC	3.86	3.93	3.80	3.50	3.32	2.70
			Index Numbers			
1. Midwestern Group - all roads, excluding C&NW and CStPM&O	115	105	120	111	110	100
2. Midwestern Group - all roads	108	101	108	103	102	96
3. Mountain-Pacific Group	100	100	100	100	100	100
4. Official Territory	104	101	111	98	100	76
5. Official Territory, excluding NYC	109	107	118	104	111	85

*Transcontinental ton-miles segregated by territories for UP, AT&SF, GN, NP, Wabash and CMStP&P.

[fol. 731]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

I.C.C. Docket No. 31503 and Sub. Nos.

Exhibit T-659 (HJB-16)

Witness: H. J. Bearss

FUNDS AVAILABLE

AND

FUNDS REQUIRED

In Response To

Exhibit MW-609—Witness John K. Langum

Exhibit E-396 — Witness Arthur Jansen

Exhibit E-409 — Witness Frank F. Coates

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[fol. 732] This exhibit has been prepared in response to the financial evidence of Witnesses Langum, Jansen and Coates. The portions of the testimony of those witnesses relating to rates of return and trends in financial indicators have been covered by my other exhibits and will not be repeated here.

I

Response to Witness Langum's Exhibit MW-609

In Exhibit MW-609, Witness Langum presents a comparison of financial statistics for certain groupings of Midwestern and Mountain-Pacific roads. Before discussing these comparisons and other features of Witness Langum's presentation in the order in which they appear in Exhibit MW-609, two basic errors common to most of the comparisons presented should be emphasized.

One is the improper grouping of roads, and particularly the exclusion of important roads operating in Midwestern territory in competition with the particular roads shown by

Witness Langum. To show the effect of this exclusion, I shall restate Witness Langum's important comparisons to include the other important Midwestern roads.

A second and most important error affecting many of the comparisons introduced in Exhibit MW-609 is the use of financial statistics reflecting substantial nonrailroad income, including oil, for the Mountain-Pacific roads. I shall discuss in the sequence in which it appears in Exhibit MW-609, Witness Langum's attempted justification for drawing upon the oil and other nonrailroad income of the Mountain-Pacific lines in making divisions of freight rates. Any such use of financial statistics in a divisions proceeding is not only improper under the Commission's decisions, but would, as a practical matter, operate to drive out of the railroad in-

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[fol. 733] dustry the oil and other nonrailroad sources of revenue.

At the outset, Witness Langum states at page 25 that he finds support for including outside income in railroad group comparisons in Witness Chandler's method of analyzing the financial results and standing of the Mountain-Pacific carriers as set forth in Exhibits T-251 and T-252, reproducing evidence introduced in the Class Rate Cases. Use of nonrailroad income in railroad group comparisons finds no support from Exhibits T-251 and T-252 because Witness Chandler did not compare one group of railroads with another group. As a consequence, the relative importance of nonoperating sources of income to different groups of roads was not of any significance. In his analysis, Witness Chandler was careful to point out that the greater part of the return received by stockholders of the Mountain-Pacific carriers was attributable to sources apart from railroad operation.

> "I might say here that as a matter of fact, moreover, the greater part of even this modest return of 2.3 percent is attributable to sources apart from the railroad operation.

"In 1953 the stockholders still would have received about two-thirds of their dividend if they had given the railroad properties away. Several of the Mountain-Pacific group in fact could pay the same dividend if they owned no railroad property at all.

"For those roads, and to a substantial extent to the eight roads as a group, the dividends may be said to arise from outside investments in oil stocks, properties, and the like, and all the retained earnings have to be plowed back into the railroad in order to keep it in operating condition." (Ex. T-251, pp. 3236-7)

It is one thing to show that *even with* both operating income and "Other Income," earnings of a group of roads are clearly below any proper standard, below the rate necessary to attract capital, and that a further reduction would be critically adverse. It is wholly another thing to compare the earnings and financial results of two groups of roads by using figures that incorporate both operating income and

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[fol. 734] "other income" and to use that comparison as a measure of financial needs arising out of railroad operations alone.

Table 1 of Exhibit MW-609 illustrates the effect of improper grouping of roads in Witness Langum's comparisons. At pages 5 through 9 of Exhibit MW-609, Witness Langum draws upon Mr. Chandler's method of analyzing the "investors' appraisal of the earnings risk" and applies it to certain groupings of Midwestern *and* Mountain-Pacific roads. His conclusion is that "the results obtained by using Mr. Chandler's approach in testing 'investors' appraisal of earnings risk' point to the significantly greater degree of earnings risk involved for investment in the Midwestern Group as compared with that in the Transcontinental Group." (p. 8).

If the investors' appraisal of the relative earnings risk places one group above another primarily because of non-railroad factors, it seems obvious that the showing cannot

fairly be used to indicate differences in the investors' appraisal of the financial results of the railroad operations. Witness Chandler, again, specifically mentioned the favorable effect of the Mountain-Pacific carriers' ownership of mineral rights or other properties, when he said:

> "Secondly, if the investor is paying for something other than future earnings, then the price may be more or less than the level at which he is capitalizing the earnings, and the capitalization rate based on that price will be distorted. For example, he may be paying something for earnings plus something extra for an interest in a natural resource in the ground which is not expected to materialize into earnings for some time to come. This second problem is of some significance with the Mountain-Pacific roads because in several instances undoubtedly the prices of their shares have been favorably influenced by ownership of mineral rights or other properties. However, this influence tends to raise the price of the stock and thus

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> [fol. 735] lower the earnings-price relationship, thereby understating the investor appraisal of the risks in the railroad itself." (Ex. T-251, pp. 3243-4)

Witness Langum's discussion of the investors' appraisal of the earnings risk attached to investment in the securities of the two groups of roads fails even to refer to this important cautionary statement of Witness Chandler's.

Apart from the impact of "other income" on Witness Langum's showing, it is misleading for three reasons: (1) the results reflect the inclusion of figures for the Missouri Pacific System, a road in reorganization until March 1, 1956; (2) the results rely heavily upon Witness Langum's grouping of roads and therefore do not reflect the investors' appraisal of Midwestern roads whose earnings will be similarly affected by Midwestern divisions; and (3) the results for more recent years substantially alter the picture that is presented.

The Commission's action in the reorganization proceeding has already established that something other than divisions was required to improve the investors' appraisal of the earnings risk involved in investing in the old Missouri Pacific System securities. The investors' appraisal of those securities is no longer of any significance since they have been replaced by new securities which have an altogether different standing in the eyes of the investing public. Any group figures that incorporate the market standing of the old Missouri Pacific System securities will be distorted and constitute an unreliable basis for making comparisons.

As to Witness Langum's exclusion of important Midwestern roads, it is obvious to me that Witness Langum's group of roads will not have different bases of divisions for themselves than for their neighboring Midwestern lines with whom they compete for traffic. For this reason, it is

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[fol. 736] improper to exclude important Midwestern roads in making the financial comparisons. I have added a group that excludes the Missouri Pacific System for reasons explained above, but includes the Texas & Pacific, the St. Louis Southwestern Railway Company, the Chicago, Burlington & Quincy Railroad, and the Texas and New Orleans Railroad. These are the remaining large Class I Midwestern carriers not included in Witness Langum's groups.

Set forth in Appendix A is a restatement of Table 1 from Exhibit MW-609, with figures excluding the Missouri Pacific System and including the other major Midwestern roads and showing the results for the seven-year period 1951 through 1957.

Referring first to the relationship between the interest paid on long-term debt and the value placed by investors on their holdings of that debt, it will be observed that exclusion of the Missouri Pacific System long-term debt reduces the Midwestern ratios by .3%. For example, the ratio shown by Witness Langum for his "Midwestern Group," that is, 4.2%, becomes 3.9% when the Missouri

Pacific System debt is excluded. Addition of the other important Midwestern roads to Langum's Midwestern groups further reduces the ratio by .2%.

Witness Langum refers to a differential of 24% in the market's appraisal of the long-term debt obligations of the Principal Contestants in the Midwestern Group as compared with its estimate of similar securities issued by seven Transcontinental Systems. When the latter group is compared with the ten Midwestern Systems, excluding the Missouri Pacific System but including the T&P, StLSW, CB&Q and T&NO, the differential in the period 1951-57 is only 9%. With the added protection afforded the Mountain-Pacific carriers' long-term debt by their larger amounts

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[fol. 737] of "other income," it is not surprising to find at least this small differential.

While the Midwestern ratios for the preferred stocks are materially reduced by the exclusion of the Missouri Pacific System, the addition of the four other Midwestern lines, and the change to 1951-57, the rates shown still exceed those for the Mountain-Pacific roads.

With respect to the common stock, it will be observed that Witness Langum's conclusion rests on percentage figures that include the results of a road in reorganization proceedings, that exclude four important Class I Midwestern roads, and that is based on the years he has selected. Without those factors influencing the results, the percentages are identical. Thus, investors accepted 12.3 cents for each dollar invested in common stock of the eight Mountain-Pacific railroads and 12.3 cents for each dollar invested in the common stock of the Midwestern Group, excluding the Missouri Pacific System and including the T&P, StLSW, CB&Q and T&NO in the period 1951-57.

When the distortions due to inclusion of the Missouri Pacific Railroad System and the exclusion of other important Midwestern roads are corrected, the relative standings of the Transcontinental and Midwestern securities are drawn much closer together, and when they are considered on the basis of the more recent 1951-57 showing,

the differences in bond and common stock showings become very slight. And this is despite the existence of substantial non-railroad income for the Mountain-Pacific lines.

Table 4 of Witness Langum compares debt at face value with equity at market value for the period 1949 through 1955. The Midwestern figures are distorted by the inclu-

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[fol. 738] sion of the Missouri Pacific securities. The Missouri Pacific Railroad Company was in reorganization until March 1, 1956. The price range of the common stock in the period from 1949 through 1955 was as follows:

Missouri Pacific Railroad Company
Common—Par $100

	1955	1954	1953	1952	1951	1950	1949
Price Range							
High	24	13½	14¼	13½	5⅝	4⅞	⅞
Low	12	7¼	6⅝	3	1¼	⅛	⅛

Source: Moody's Transportation Manual

The Commission has already concluded that other steps were needed to remedy the capitalization structure of the Missouri Pacific, so that the use of data reflecting the old securities of the Missouri Pacific is improper in this division proceeding.

At pages 18 to 25 of Exhibit MW-609, Witness Langum presents a showing which he candidly recognizes is based not only on railroad operations, but as well upon the Transcontinental Group's "greater income from other sources." (p. 21). Presumably this showing was intended to add evidence with some weight to a record filled with evidence of the comparative earnings from railroad operations. This showing would have persuasiveness only if it helped in some way to indicate that the Midwestern lines should have some additional dollars in their divisions of railroad rates because the Transcontinental carriers had "greater income from other sources." Otherwise a record made up of comparative railroad operating income would provide all the necessary evidence needed to decide the issues of the case. What Witness Langum is saying, in substance, is that his clients are entitled to an increase in their divisions out of

the "Other Income" of the Transcontinental roads. The necessary effect of Witness Langum's comparisons is to

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[fol. 739] make a claim against the Transcontinental carriers' income from other sources.

A partner in a firm of economic consultants would have to be an exceedingly bold man indeed if he claimed part of the profits when his associate individually opened a new grocery store, using his own money, assuming the whole of the risk himself and using only his own know-how and without consulting with his partner in any fashion. Certainly there is no better foundation for a claim to the profits or "Other Income" if the partners happen to be railroads participating in joint rates, but individually engaged in their separate ventures that produce the "Other Income."

Witness Langum endeavors to overcome this problem in two ways: (1) by classifying anything a railroad undertakes to do as "closely associated with railroad operations," and (2) by contending that subsidiary and auxiliary sources of other income cannot be divorced financially from the railroad. As I shall show, Witness Langum's position, which has been rejected by the Commission, is factually incorrect.

The Interstate Commerce Commission has taken the position, which I believe to be sound, that "Other Income" has no place in a divisions proceeding.

Official-Southern Divisions, 287 I.C.C. 497, 505:

> "The comparison of 'other income' received by the two groups of railroads, dividends paid, and fixed charges, submitted by the southern lines, in our opinion are not pertinent. What we must consider under section 15(6) is 'the amount of revenue required to pay their respective operating expenses, taxes, and a fair return on their railway property held for and used in the service of transportation.' This amount is measured by net railway operating income." *

* See also *Class Rate Investigation, 1939,* 262 I.C.C. 447, 614.

[fol. 740] *Official-Southwestern Divisions,* 287 I.C.C. 553, 654-5:

> "The southwestern lines ask consideration of the fact that the Pennsylvania has certain investments in affiliated companies from which it receives dividends. The amounts so received are reported in the income accounts as 'other income' and are not included in net railway operating income. Nonoperating income, received from other than transportation service, is not taken into account in passing upon rates for transportation service, and we do not consider it of material importance in this proceeding, *Class Rate Investigation, 1939,* 262 I.C.C. 447, 614."

Class Rate Investigation, 1939, 262 I.C.C. 447, 614:

> "The rate of return in the southern region has exceeded that in the eastern district in 4 years out of the 6-year period 1936-1941, and in 5 years out of the 7-year period 1936-42. The rate in 1943 was less than in 1942, but the rate of return in the southern region exceeded that in the eastern district. Nonoperating income of the eastern carriers is relatively much greater than that of the southern carriers, and if taken into account would indicate a higher return in the East. However, nonoperating income does not provide a test of relative transportation costs, rates, or of operating efficiency."

As these citations show, the Commission has clearly ruled out "Other Income" as a factor to be considered in comparing financial results of different groups of carriers in a divisions proceeding. Accordingly, a showing of comparative earnings that includes the income from other sources is not pertinent to this case.

Moreover, Witness Langum has quite missed the point in Exhibit T-275 when he attempts to sweep everything operating under a corporate name into the "Transportation

Operations" category. In an effort to eliminate issues and to state the case conservatively, the income from refrigerator-car lines and Pullman Company operations was included in our statements dealing with the source and application of funds. The essential characteristic of both of these operations that seemed to justify this treatment was that the revenues and expenses occur in connection with the railroad operations on both groups of roads.

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[fol. 741] Contentions as to the degree to which expenses matched revenues on each group of roads could be eliminated by simply including both sides of the ledger in the funds available and funds required statements. Having taken this step in the interest of eliminating controversy, it comes as something of a surprise to find a Midwestern witness claiming that the Transcontinental lines' "greater income from other sources" must be considered as part of a comparison of the funds available even though his clients provided none of the capital, assumed none of the risk, and contributed none of the know-how involved in the various enterprises. Even if these enterprises were making a profit and were "closely associated with railroad operations," they certainly provide no basis for adding an increment to the divisions of the Midwestern carriers above what they would be entitled to had the Transcontinental carriers no outside income whatsoever.

In addition, Witness Langum is factually incorrect. As the first separately listed "Important Source of 'Other Income'," he includes the following:

> "Separately incorporated motor-carrier operations, both supplementary and complementary in nature with regard to the rail operations." (p. 24)

Appendix B lists the dividends received from motor-carrier subsidiaries of the Mountain-Pacific roads in the postwar period. Down through 1952, certain of the carriers received small amounts from bus operations. Since 1952 no Mountain-Pacific road has received any dividends from their separately incorporated motor-carrier operations. Whether

or not the Midwestern roads are correct in their contentions with respect to motor-carrier operations is a matter of academic interest, for they have produced no income in recent years.

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[fol. 742] Witness Langum next lists pipe line companies and mentions in particular that owned by the Southern Pacific Company on the basis that it is located on the railroad right of way. He does not explain why the success or failure of these pipe line ventures should influence the Commission to adjust Midwestern divisions upwards or downwards. The brief reference to pipe line companies does not indicate that Witness Langum was aware of the fact that substantial portions of the pipe line operated by the Southern Pacific Pipe Line Company are not on the railroad right of way. Do the Midwestern lines claim a right to increased divisions as a result of pipeline operations wholly or in part removed from the railroad right of way? The outer reaches of the phrase "closely associated with railroad operations" are not defined, but the tenor of the remarks and the ambiguity of the phrase indicate virtually no limits. Furthermore, I find no offer on the part of the Midwestern lines to bail the Southern Pacific Company out should this venture prove in the long run to have been an economic failure. It is also significant that again Witness Langum has failed to check his source material, for the fact is that the Southern Pacific Pipe Line Company has not paid a dividend yet.

Next, Witness Langum mentions the "Union Pacific's large oil production," asserting that it is "primarily derived from its railroad terminal property in the Los Angeles Harbor area, that area being located in the very heart of the prolific Wilmington Oil Field." (p. 24). The fact is that the land mentioned is *not* operating property. In the year 1903, the San Pedro, Los Angeles and Salt Lake Railroad acquired the Los Angeles Terminal Land Company and thereby became the owner of all of its *nonoperating*

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[fol. 743] lands. These nonoperating lands include the land now known as the Wilmington Oil Field. More than 90%

of the railroad land holdings in this area is nonoperating property. Moreover, nearly a third of the Union Pacific's production is from oil fields in Colorado and Wyoming, which are located some distance from the railroad operations. For example, the important Rangeley Field in Colorado is 230 miles from the railroad.

Finally, Witness Langum mentions the income derived from investments in subsidiary railroad companies. Some of his clients made this same argument in the Official-Southwestern Divisions case with respect to the investment of the Pennsylvania in affiliated companies. As we have seen, the Commission rejected the contention. If Witness Langum's contrary position were upheld, we would have the unusual situation of the Midwestern lines obtaining higher divisions because the earnings of the Burlington or Cotton Belt were high, although the reasons for the high earnings of these roads are that the Midwestern lines' divisions on transcontinental traffic are already too high.

Another phase of Witness Langum's position is that it is not possible to divorce the nonrailroad from the railroad sources of income. He said:

> "It would not be possible, from a financial standpoint, to divorce from these railroad companies the various subsidiary and auxiliary sources of income which are so closely associated with their direct rail operations. In fact, such subsidiary and auxiliary operations are actually a part of the over-all transportation enterprise in which each of these predominant members of the Transcontinental Group is engaged." (MW-609, p. 25)

This phase is equally lacking in factual support. The Commission has said that it is obligated under Section 15(6) to

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[fol. 744] consider " 'the amount of revenue required to pay their respective operating expenses, taxes, and a fair return on their railway property held for and used in the service of transportation.' This amount is measured by net railway operating income." I find nothing in Witness

Langum's paragraph on this subject which gives in detail the deficiencies in the separation of operating from non-operating income provided for in Uniform System of Accounts, nor any explanation why the net railway operating income figure does not constitute the measure which the Commission said it does. The accounting procedures called for by the Uniform System of Accounts make possible a segregation of the financial results of railroad from non-railroad operations that is meaningful.

Furthermore, I find no factual support for his opinion that it would not be possible from a financial standpoint to divorce the various subsidiary and auxiliary sources of income from the railroad operations. Desirable as it may be under normal circumstances for a railroad to diversify and thus provide the whole enterprise with a more stable earnings base, if success with the associated ventures carries with it an obligation to share with neighbors the financial fruits of assuming the risks, financial wisdom will dictate a quick divorce from present operations and a long hard look before future marriages are undertaken. As Witness Lovett testified on behalf of my road:

> "The question of complete corporate segregation or distribution to the stockholders of the oil properties has been under constant review. Its effect on Union Pacific financial condition and statements, while dramatizing the facts I have here set forth and thereby making the railroad's need for relief more easily apparent, has so far been considered unwise for a variety of reasons, including tax problems." (T-267, pp. 8-9)

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[fol. 745] I am sure the Southern Pacific Company and the other Mountain-Pacific carriers with large amounts of nonoperating income would similarly have to give serious consideration to spinning off these activities if such contentions as that made by Witness Langum were ever given serious consideration. One way of making crystal clear the degree to which transcontinental carriers rely upon adequate divisions would be to "divorce" the various sub-

sidiary sources of income and put beyond question the fact that they were not available as sources of funds to be tapped by other carriers, directly or indirectly. After the segregation of properties, the carriers would be in a position to come back to the Commission for a proper basis of divisions that related entirely to the railroads' operations jointly performed for the involved traffic. It seems obvious why the Commission would not want to encourage such steps and why the holdings quoted above are that financial comparisons incorporating nonoperating results are not pertinent. Certainly forcing the segregation of sources of "Other Income" would be taken at a high cost to the public interest and, as a matter of fact, to the long-term interest of the Midwestern and Eastern lines.

Having reviewed this portion of Witness Langum's testimony, it is of interest to see whether it fits into the treatment given "Other Income" in other portions of his own testimony and in the testimony of other Midwestern witnesses. Witness Kleinsorge advocated the elimination of the federal income tax on "Other Income" as an item of expense in Exhibit MW-85, page 4. As Witness Langum points out in the first volume of his testimony, MW-608, page 32, there is unanimity of opinion as to the necessity for the adjustment. It is impossible for me to follow Wit-

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[fol. 746] ness Langum's reasoning when, on the one hand, he advocates elimination of the effect of Federal Income Tax on Other Income, while at the same time in the second volume of his testimony claiming that "Other Income" should be considered by the Commission as a source of funds, and that these "subsidiary and auxiliary operations are actually part of the overall transportation enterprise." (MW-609, p. 25). The Midwestern lines can't have it both ways. The Mountain-Pacific carriers, on the other hand, have taken a consistent position of eliminating the federal income tax on other income and of excluding outside income when considering the financial results of the railroads' operations.

At pages 25 through 31 of Exhibit MW-609, Witness Langum discusses the "Expanding Midwestern Economy Brings Substantial Capital Needs for Midwestern Group." The factual support offered to prove this assertion consists of tables showing comparative growth trends in terms of total population, total personal income and total nonagricultural employment. How these figures translate themselves into a need for railroad capital expenditures of a given amount is not spelled out in the testimony. We are left with the general observation that everybody needs to make capital expenditures. His own Table 6 shows that the eight Mountain-Pacific roads spent $1,544 million on gross additions and betterments as compared with only $885 million in the 1949-1953 period by the Midwestern Group. With a 41 percent greater average book investment, these carriers expended 74 percent more on gross additions and betterments (MW-609, pp. 20-21).

In spite of the figures set forth in Tables 7, 8 and 9, Witness Langum admits that "The percentage of relative economic growth in Mountain-Pacific Territory has been greater, and no doubt this will continue to be the case, than

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[fol. 747] in Midwestern Territory." (p. 26). The figures in the preceding paragraph show that this growth has been accompanied by a much larger demand for capital improvements. The increase in AAR net investment from 1947 to 1955, using Witness Kleinsorge's grouping, amounted to $464 million for the Midwestern Group as compared with $1,186 million for the Transcontinental Group. (Ex. MW-218, p. 2, and Ex. MW-449, p. 2).

It is difficult to follow the thread of his contentions when different parts of his testimony are considered together. Although pointing out at page 30 that the absolute increase in population in the postwar period in Mountain-Pacific Territory just barely exceeded that in Midwestern Territory, that the dollar increase in total personal income in Midwestern Territory exceeded that in Mountain-Pacific

Territory, and that the increase in the number of employees in nonagricultural establishments in Midwestern Territory exceeded that in Mountain-Pacific Territory, on pages 42 through 46 he is demonstrating that in the very same period the tons and ton-miles of freight handled by the Transcontinental Group had grown at a greater rate than for the Midwestern Group. Presumably, relative growth in the volume of business handled by the railroads has a relationship to the relative demand for capital expenditures, as Witness Langum points out. (p. 26).

Finally, it is difficult to reconcile the logic of Witness Langum's position with that of Witness Carpenter. If "the need for capital expenditures measured in dollars relates to the amount of growth rather than the percentage rate of growth," (Ex. MW-609, p. 26), and Witness Carpenter demonstrates in his Exhibits MW-149, 153, 223, 224 and 231 that the greatest increase in revenue ton-miles has taken place in Mountain-Pacific Territory in the past and

[fol. 748] that that growth characteristic will continue in the future (Tr. 3157), it should follow that Mountain-Pacific carriers will require proportionately larger amounts of capital expenditures.

With respect to the material on pages 37 through 50 of Witness Langum's Exhibit MW-609, my Exhibits T- ..... (HJB-12) and T- ..... (HJB-13) set forth a comparison of the trends in operating revenues, ton-miles and rates of return for the Midwestern and Mountain-Pacific roads. Additional evidence on the relative rates of return will be found in my Exhibits T- ..... (HJB-9) and T- ..... (HJB-10).

At page 52 of Exhibit MW-609, Witness Langum comments on a comparison of transportation and operating ratios. Witness Boles pointed out at page 6 of Exhibit T-350 that the Chicago and North Western Railway Company transportation ratio was materially out of line with its other Midwestern neighbors. A new management took over on April 1, 1956, with a program of modernization and

mechanization of the property. Set forth below are the transportation and operating ratios for the Chicago and North Western System in the postwar years.

	Chicago and North Western System	
Year	*Transportation Ratio*	*Operating Ratio*
1946	45.18	85.44
1947	44.43	83.65
1948	45.02	84.53
1949	48.08	89.93
1950	44.88	83.89
1951	47.24	88.00
1952	46.14	86.22
1953	44.85	86.10
1954	46.70	88.13
1955	45.30	84.63
1956	46.70	87.82
1957	44.58	85.44
1958	42.81	82.85

Source: Annual Report Form A to I.C.C.—Years 1946 through 1957.
Forms R&E filed with I.C.C.—Year 1958

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[fol. 749] Even though 1958 was a recession year for business, it will be observed that the C&NW System achieved the lowest transportation and operating ratios that it has experienced in the thirteen postwar years. One of the factors that obviously has affected the relative transportation and operating ratios for these groups has been the abnormally high ratios for the C&NW System.

Tables 18 and 19 of Exhibit MW-609 compare adjusted net railway operating income with total operating revenues for the seven Transcontinental Systems and the ten Midwestern Systems. As in so much of Witness Langum's testimony, the results of his showing rest on his selection

of the carriers to be used in his groups. When proper groupings of the carriers are used, the results are completely changed. In Appendix C I have set forth the figures for the year 1956, in the same format used by Witness Langum but with the carriers grouped in the way they have been grouped in my rate of return exhibits. Looking first at the restatement of Table 18, it will be noted that, whereas the ten Midwestern Systems were shown with a ratio 15 index points below the seven Transcontinental Systems by Witness Langum, this table shows the Mountain-Pacific Territory-all roads to have an index of only 94 when compared with Midwestern Territory-all roads, excluding C&NW and CStPM&O, and an index of 104 when compared with Midwestern Territory-all roads. The restatement of Table 19 shows that the index of Mountain-Pacific Territory-all roads is below that for either of these Midwestern groups, in the same order being 88 and 99.

Pages 56 through 60 require no further comment beyond what has already been said about the lack of pertinency of figures that rest in large part upon a comparison of the relative amounts of "Other Income."

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[fol. 750] The material at pages 60 through 69 has already been dealt with at pages 28 through 31 of my Exhibit T- ..... (HJB-9).

In attempting to deal with the showing as to funds available and funds required from transportation operations as presented by the Transcontinental roads, Witness Langum makes the flat assertion on page 76 that "Retained Earnings Benefit the Stockholders." In the subsequent paragraphs I find no explanation of how retained earnings benefited the stockholders of the Transcontinental roads when they received no return on the retained earnings. An investment that produces no return over a period of years cannot be considered beneficial.

Again at page 80 it is said: "The basic philosophy that capital expenditures should somehow be treated in the

same category as operating expenses when evaluating the position of stockholders with respect to earnings on their investment, and that any increase in their investment, through plowed-back earnings, should be completely disregarded, is simply an erroneous interpretation of the facts of business finance and investment decision in the present-day American economy." Witness Jansen, the expert financial witness for the East, reached the opposite conclusion in the course of cross-examination. From the quotation of his cross-examination on page 29 of this statement, it is clear that he recognized the expenditure of $800 million for added net investment with no return as constituting simply a part of the real cost of serving Mountain-Pacific territory.

At pages 77-8 it is stated that "Leaving out of consideration that part of the capital expenditures accomplished through borrowings (new money) greatly distorts comparisons when one group uses comparatively heavy bor-

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[fol. 751] rowings for this purpose while another group, such as the Principal Contestants in the Transcontinental Group, has need to borrow comparatively little." Witness Langum has quite evidently not studied Exhibit T-275 closely enough. Both sides of the ledger are provided for with respect to equipment obligations. Item 4a in the tables includes the funds required to meet installment payments on equipment obligations and item 4(b) includes the funds made available from equipment obligations. Item 2 provides for the interest payments necessary in connection with equipment obligations. Consequently, any capital expenditures accomplished through borrowings under equipment obligations are fully recognized and provided for.

Witness Langum appears to recognize that bond issues that simply represent a refinancing of old issues do not provide new money for capital expenditures. Item 4b on page 4 of Exhibit T-275 indicates that there were no bonds issued by Midwestern roads in the ten-year period 1946 through 1955 for capital expenditures as contrasted

with refinancing. As a matter of fact, that item shows that the Mountain-Pacific roads issued $3,682,000 of bonds in this ten-year period that were not for refinancing purposes. If his point had any merit, the advantage, therefore, would be against his clients in this case. The point has no merit, however, because provision is made in Item 2 for the transportation portion of funds required for fixed charges and contingent interest. The cost of new money for capital expenditures in the form of bonds is uniformly provided for in all territories, if any is secured in this fashion.

Witness Langum attempts to obscure the effect of the funds available and funds required showing by his group-

[fol. 752] ing of the data in Table 25 of Exhibit MW-609. In order to lay at rest some of the assertions made in connection with that table, I have included as Appendix D a recomputation of Table 25 showing the results both before and after acquisition adjustment, on both the I.C.C. Valuation Base and the Book Value Base and for additional groupings of carriers.

After examining the figures for the ten-year period 1946 through 1955 selected by Witness Langum, it is apparent that the Midwestern ratios are more favorable than the ratios for the Mountain-Pacific or Transcontinental roads, regardless of the treatment of acquisition adjustment or the base used, with one exception. That exception occurs when the Midwestern Group is improperly limited to contestant roads. The ratios in line 2 exceed the ratios in line 1 in every instance. The ratios in line 6 exceed the ratios in line 3 in every instance. The ratios in line 8 exceed the ratios in line 7 in every instance. It is also important to note from lines 6(a) and 8(a) that when the abnormally low results of the C&NW System are excluded, the ratios of the Midwestern groups are increased. As the C&NW System regains its normal earning power and is in line with its other neighbors, the Midwestern ratios will more nearly approximate those shown in lines 6(a) and 8(a).

It is only when the Midwestern Group is improperly confined to the contestant roads that the relative showing is changed. In that connection, it is of interest to note that Witness Langum has included the results for the Texas & Pacific in computing the figures shown on lines 4 and 5 for "Principal Contestants in the Midwestern Group" and "Principal Contestants in the Midwestern Group, plus CMStP&P." Although the Texas & Pacific is not listed as a Midwestern complainant road, I presume

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[fol. 753] that Witness Langum included the T&P in his Table 25 group of Midwestern roads on the entirely logical assumption that the divisions prescribed for this area would apply to the Texas & Pacific. For the same reasons, the other roads operating as neighbors of the Midwestern contestants should be included in such showings as these.

[fol. 754]

APPENDIX H
Page 1 of 2 Pages

PERCENTAGES OF FUNDS AVAILABLE TO STOCKHOLDERS FROM TRANSPORTATION OPERATIONS
TO NET INVESTMENT IN PROPERTY USED IN TRANSPORTATION SERVICE
Weighted on Transcontinental Ton-Miles - Territorial Method 1/

Item 3, Page 5 - Exhibit T-275

All Territories Compiled on Same Basis 2/

A. Annual Average - Five Year Period

Groups (1)	Average 1951 - 1955 Weighted Percentage Of Funds Available (2)	Average 1951 - 1955 Index Numbers (MP = 100) (3)	Average 1952 - 1956 Weighted Percentage Of Funds Available (4)	Average 1952 - 1956 Index Numbers (MP = 100) (5)	Average 1953 - 1957 Weighted Percentage Of Funds Available (6)	Average 1953 - 1957 Index Numbers (MP = 100) (7)
1. Principal Mountain Pacific Roads	1.85	100	1.99	100	2.01	100
3. Principal Midwestern Roads	1.94	105	2.06	104	1.98	99
4. Principal Midwestern Roads, excluding C&NW	2.09	113	2.23	112	2.20	109
5. Principal Official Territory Roads	2.48	134	2.54	128	2.43	121
6. Principal Official Territory Roads, excluding NYC	2.75	149	2.83	142	2.73	136

B. Annual Average - Eight Year Period

	Average 1948 - 1955		Average 1949 - 1956		Average 1950 - 1957	
1. Principal Mountain Pacific Roads	1.73	100	1.91	100	2.04	100
3. Principal Midwestern Roads	2.06	119	2.06	108	2.09	102
4. Principal Midwestern Roads, excluding C&NW	2.21	128	2.24	117	2.30	113
5. Principal Official Territory Roads	2.37	137	2.34	123	2.44	120
6. Principal Official Territory Roads, excluding NYC	2.65	153	2.58	135	2.76	135

C. Annual Average - Ten Year Period

	Average 1946 - 1955		Average 1947 - 1956		Average 1948 - 1957	
1. Principal Mountain Pacific Roads	1.96	100	1.99	100	1.87	100
3. Principal Midwestern Roads	2.24	114	2.19	110	2.07	111
4. Principal Midwestern Roads, excluding C&NW	2.35	120	2.37	119	2.26	121
5. Principal Official Territory Roads	2.37	121	2.39	120	2.30	123
6. Principal Official Territory Roads, excluding NYC	2.60	133	2.65	133	2.63	141

1/ Percentages shown on Page 1 of Appendix A, weighted on territorial method (weighting factors shown on Page 2 of Appendix H).

2/ All Territories Compiled on Same Basis means the Mountain Pacific Roads have been compiled on same basis as the Midwestern and Official Territory Roads were compiled in Exhibit T-275.

APPENDIX H

Page 2 of 2 Pages

TERRITORIAL METHOD WEIGHTING FACTORS

Principal Mountain Pacific Roads

Road	Ton-Miles Transcontinental Traffic (000)	Percent of Total
(1)	(2)	(3)
AT&SF	6 682 316	14.14
CMStP&P	1 487 786	3.15
D&RGW	3 557 679	7.53
GN	3 971 215	8.40
NP	4 210 640	8.91
SP	15 226 888	32.23
UP	10 428 226	22.07
WP	1 686 635	3.57
Total	47 251 385	100.00

Principal Midwestern Roads

Road	Ton-Miles Transcontinental Traffic (000)	Percent of Total Including C&NW	Percent of Total Excluding C&NW
(1)	(2)	(3)	(4)
CB&Q	4 784 785	11.43	12.15
CRI&P	3 964 232	9.47	10.06
IC	1 040 904	2.49	2.64
MP	2 926 871	6.99	7.43
StL-SW	1 189 136	2.84	3.02
T&NO	2 300 784	5.50	5.84
T&P	1 044 233	2.50	2.65
AT&SF	6 354 819	15.19	16.13
CMStP&P	2 277 042	5.44	5.78
GN	2 356 367	5.63	5.98
NP	1 949 105	4.66	4.95
UP	8 545 000	20.42	21.69
Wabash	663 613	1.59	1.68
Total (excl. C&NW)	39 396 891	xx	100.00
C&NW	2 447 563	5.85	xx
Total (incl. C&NW)	41 844 454	100.00	xx

Principal Official Territory Roads

Road	Ton-Miles Transcontinental Traffic (000)	Percent of Total Including NYC	Percent of Total Excluding NYC
(1)	(2)	(3)	(4)
B&O	1 276 826	11.49	15.04
C&O	631 728	5.69	7.44
Erie	1 530 830	13.78	18.04
NYC&St L	1 184 398	10.66	13.95
Penn	2 932 611	26.40	34.55
Wabash	880 560	7.92	10.38
CMStP&P	50 924	.46	.60
Total (excl.NYC)	8 487 877	xx	100.00
NYC	2 622 223	23.60	xx
Total (incl.NYC)	11 110 100	100.00	xx

SOURCE: Ton Miles Transcontinental Traffic from Exhibit T-311, Mountain Pacific Lines Traffic Study, restated to include all Milwaukee transcontinental ton miles from Exhibit TM-394 (expanded to an annual basis). (Exhibit T-___(HJB-10), Appendix B)

[fol. 756]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Exhibit No. E-700 (JLH-8)

Witness: J. L. Heywood

(Supplement to Exhibit No. E-504)

Docket 31503

OFFICIAL—TRANSCONTINENTAL DIVISIONS

RAIL COSTS

Unit Cost Factors

	Service Unit	Fresh Fruits and Vegetables - Eastbound (16 Tons-Refrigerator Car) Eastern District	Fresh Fruits and Vegetables - Eastbound (16 Tons-Refrigerator Car) Western District	All Other Traffic (27.7 Tons-Box Car) Eastern District	All Other Traffic (27.7 Tons-Box Car) Western District
1939					
Terminal	Hundredweight	3.1¢	3.3¢	2.6¢	2.9¢
Line Haul	Hundredweight mile	0.071250	0.064950	0.038010	0.037240
1943					
Terminal	Hundredweight	3.9	4.0	2.8	2.9
Line Haul	Hundredweight mile	0.068244	0.059592	0.035362	0.033659
1946					
Terminal	Hundredweight	4.8	4.7	3.4	3.3
Line Haul	Hundredweight mile	0.085582	0.073304	0.043066	0.039789
1948					
Terminal	Hundredweight	5.3	5.2	3.7	3.7
Line Haul	Hundredweight mile	0.095957	0.081241	0.050297	0.043916
1950					
Terminal	Hundredweight	6.0	5.6	4.3	3.9
Line Haul	Hundredweight mile	0.107350	0.088545	0.055911	0.045582
1952					
Terminal	Hundredweight	7.3	7.1	5.3	5.0
Line Haul	Hundredweight mile	0.112265	0.091956	0.059094	0.048200
1953					
Terminal	Hundredweight	7.4	7.2	5.4	5.0
Line Haul	Hundredweight mile	0.126227	0.104304	0.059904	0.049429
1954					
Terminal	Hundredweight	7.9	7.4	5.8	5.3
Line Haul	Hundredweight mile	0.128435	0.105326	0.060271	0.048997
1956					
Terminal	Hundredweight	8.0	7.7	5.8	5.4
Line Haul	Hundredweight mile	0.128476	0.102003	0.058874	0.049085
1957					
Terminal	Hundredweight	8.8	8.4	6.5	6.0
Line Haul	Hundredweight mile	0.138601	0.107910	0.063661	0.052066

The above unit cost factors are the basis for the charts and cost scales on the following five pages. The cost factors result from the application of Rail Form A "Formula for use in Determining Rail Freight Service Costs" as more fully described on the respective page

Comparison of Composite Rail Costs for All Cars
24.8 Ton Average Load-All Traffic 1/

[fol. 758]

Fully Distributed Costs *Excluding Passenger and Less Carload Deficiencies Increased 11% to Reflect Circuity

Miles	Year 1953		Year 1956		Year 1957	
	Eastern District	Western District	Eastern District	Western District	Eastern District	Western District
50	9.1¢ per Cwt.	8.2¢ per Cwt.	9.6¢ per Cwt.	8.6¢ per Cwt.	10.6¢ per Cwt.	9.3¢ per Cwt.
100	12.7	11.1	13.1	11.4	14.4	12.4
150	16.2	13.9	16.7	14.3	18.2	15.4
200	19.8	16.8	20.2	17.2	22.0	18.5
250	23.3	19.7	23.7	20.0	25.8	21.5
300	26.8	22.6	27.2	22.9	29.6	24.5
350	30.4	25.5	30.8	25.7	33.4	27.6
400	33.9	28.3	34.3	28.6	37.3	30.6
450	37.4	31.2	37.8	31.5	41.1	33.7
500	41.0	34.1	41.3	34.3	44.9	36.7
550	44.5	37.0	44.9	37.2	48.7	39.8
600	48.1	39.9	48.4	40.1	52.5	42.8
650	51.6	42.7	51.9	42.9	56.3	45.8
700	55.1	45.6	55.4	45.8	60.1	48.9
750	58.7	48.5	59.0	48.7	63.9	51.9
800	62.2	51.4	62.5	51.5	67.7	55.0
850	65.7	54.2	66.0	54.4	71.5	58.0
900	69.3	57.1	69.5	57.2	75.3	61.0
950	72.8	60.0	73.1	60.1	79.1	64.1
1000	76.4	62.9	76.6	63.0	82.9	67.1
1050	79.9	65.8	80.1	65.8	86.7	70.2
1100	83.4	68.6	83.6	68.7	90.5	73.2
1150	87.0	71.5	87.1	71.6	94.3	76.2
1200	90.5	74.4	90.7	74.4	98.2	79.3
1250	94.0	77.3	94.2	77.3	102.0	82.3
1300	97.6	80.2	97.7	80.2	105.8	85.4
1350	101.1	83.0	101.2	83.0	109.6	88.4
1400	104.7	85.9	104.8	85.9	113.4	91.4
1450	108.2	88.8	108.3	88.7	117.2	94.5
1500	111.7	91.7	111.8	91.6	121.0	97.5
1550	115.3	94.6	115.3	94.5	124.8	100.6
1600	118.8	97.4	118.9	97.3	128.6	103.6
1650	122.4	100.3	122.4	100.2	132.4	106.7
1700	125.9	103.2	125.9	103.1	136.2	109.7
1750	129.4	106.1	129.4	105.9	140.0	112.7
1800	133.0	109.0	133.0	108.8	143.8	115.8
1850	136.5	111.8	136.5	111.6	147.6	118.8
1900	140.0	114.7	140.0	114.5	151.4	121.9
1950	143.6	117.6	143.5	117.4	155.2	124.9
2000	147.1	120.5	147.1	120.2	159.1	127.9
2050	150.7	123.4	150.6	123.1	162.9	131.0
2100	154.2	126.2	154.1	126.0	166.7	134.0
2150	157.7	129.1	157.6	128.8	170.5	137.1
2200	161.3	132.0	161.2	131.7	174.3	140.1
2250	164.8	134.9	164.7	134.6	178.1	143.1
2300	168.3	137.8	168.2	137.4	181.9	146.2
2350	171.9	140.6	171.7	140.3	185.7	149.2
2400	175.4	143.5	175.2	143.1	189.5	152.3
2450	179.0	146.4	178.8	146.0	193.3	155.3
2500	182.5	149.3	182.3	148.9	197.1	158.4

* Out of Pocket and Constant Costs including 6% Return on Investment based on application of Rail Form A "Formula for use in Determining Rail Freight Service Costs" prepared by the Cost Finding Section, Bureau of Accounts, Cost Finding and Valuation of the I.C.C. Loss and Damage not included. Composite Costs are based on percentages of Equipment from Kihn's Exh. T-310. Return on Investment based on I.C.C. Elements of Value.

1/ Based on Kihn's Exh. T-310.

[fol. 759]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Doc. No. 31503 & Sub Nos.

Exhibit No. MW-737 (JKL-3)

Witness: John K. Langum

TRANSCONTINENTAL DIVISIONS CASES

Additional Testimony of

JOHN K. LANGUM

[fol. 760]

Additional Testimony of John K. Langum

In his Exhibits T-652, T-653, T-655, T-656, T-657, and T-660, Mr. Bearss has set up additional comparisons of rate of return for his various groups of railroads and has extended the statistical data of his previous exhibits through 1957. In his supplemental testimony on behalf of the Eastern railroads recently distributed for presentation at this hearing, Mr. Jansen has brought up to date through 1958 certain portions of the material contained in his Exhibits E-396 and E-397.

Additional comparisons of earning power and rate of return extended through 1958 are presented in this exhibit as set forth in Appendix A. The appended tables are reproductions of those having corresponding numbers in my Exhibit MW-608 with 1958 data added. The letter "a" has been added to each table number to distinguish it from the corresponding table in Exhibit MW-608.

Superior Earnings Performance of Transcontinental Group in Direct Railroad Operations

The comparisons of earning power and rate of return in this exhibit, as in Exhibit MW-608, are solely and exclusively in terms alone of direct railroad operations.

Comparison of the data for the years 1957 and 1958 shows that the advantage of the Transcontinental Group over the Midwestern Group in earning power and rate of return was maintained, and, in fact, quite generally in-

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[fol. 761] creased in the later year. The trend of expansion in this advantage in the later post-war years, which was a market feature of the data in 1957, is thus shown as continuing through 1958.

In earning power and rate of return from direct railroad operations the Transcontinental Group continues to stand far out ahead of the Midwestern Group.

Comprehensive Comparisons

As in Exhibit MW-608, comprehensive comparisons have been made of earning power and rate of return data for the three Contestant Groups of railroads in these proceedings. Similar comparisons have been made as to quite different groupings which have been used by Mr. Bearss and for certain modifications of such groupings. Corresponding data have also been shown for the principal railroads in each of the contestant groups.

Likewise, as in Exhibit MW-608, measurements from several standpoints have been included in these studies of earning power and rate of return. Efforts again have been made to utilize all commonly used concepts of net railway operating income, the bases to which these magnitudes are related, and methods of averaging the ratios derived.

For reasons explained in my previous testimony, it is my opinion that these are the primary significant data and procedures for making group comparisons in this proceeding. Brought up to date through 1958, they continue to lead to conclusions quite the opposite of those expressed by Mr. Bearss.

[fol. 762] Effect of 1958 Recession

As noted by Mr. Jansen, the much greater dependence of the Eastern roads on heavy industrial activity and the movement of coal caused their freight and total revenues to decline much more severely than those of the Transcontinental roads. Accordingly, earning power and rate of return figures for the Eastern roads likewise showed sharp declines in 1958.

In appraising these data for the Eastern roads, their greater volatility in rate of return in response to cyclical changes in industrial production, previously noted on page 49 of my MW-609, must be borne in mind. With full recovery throughout the entire range of industrial production, the Eastern roads may be expected to show a marked rebound in earning power and rate of return in keeping with past experience.

In 1958, measurements of earning power and rate of return for both the Transcontinental Group and the Midwestern Group show improvement in 1958 over 1957. Generally speaking, the extent of this improvement is shown to have been greater for the Transcontinental Group than for the Midwestern Group. The superiority of the Transcontinental Group over the Midwestern Group in earning power and rate of return from direct railroad operations was very definitely maintained.

[fol. 763]

BEFORE THE
INTERSTATE COMMERCE COMMISSION

Doc. No. 31503 & Sub Nos.
Exhibit No. MW-738 (JKL-4)
Witness: John K. Langum

TRANSCONTINENTAL DIVISIONS CASES

Additional Testimony of
JOHN K. LANGUM

[fol. 764]

Additional Testimony of John K. Langum

In additional testimony set forth in Exhibit MW-737 (JKL-3) partial response was made to certain of a series of additional exhibits of Mr. Bearss. In this additional testimony, MW-738 (JKL-4), further response is made to the entire series of exhibits running from T-652 through T-660 and primarily to T-652 and T-659.

Rate of Return Comparisons

Mr. Bearss in his "response to Exhibits MW-608 and MW-609" (Exhibit T-632) dealt first with the MW-608 rate of return figures on the Book Value base by setting up similar data on some of his own groupings *for the years 1955, 1956 and 1957* only.

Improper Groupings and Concepts

It is significant that he made no use of the actually contending groups of railroads. He continued to make

improper comparisons, in my judgment, by including the Milwaukee in his so-called Mountain-Pacific group, by including in the Midwestern Group subsidiaries of Transcontinental roads, and by "excluding C&NW and CStPM&O" from the Midwestern Group. These improper groupings, of course, enabled him to show higher rates of return for his Midwestern groups. The reasons for my opinion that these groups are improper were set forth in MW-608, pp. 7-26, and need no repeating here.

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[fol. 765] Likewise, in some of his tables Mr. Bearss again deducts the acquisition adjustment account from the investment base. I continue to regard this as improper as stated in MW-608, pp. 27-29 and Appendix B.

Mr. Bearss again attacked the Elements of Value base. This was, in large part, a revival of his previous general attack upon use of the ICC Valuation base, derived from the "Elements of Value Statements" published annually by the Commission. Mr. Bearss asserted that "no Commission decision has been cited which *adopts* the so-called Elements of Value base *as its uniform method* of establishing the value of all railroads for rate making purposes". (Emphasis supplied) However, he indicated his familiarity with the Commission's use of this base in computing rates of return in the general revenue cases, which he referred to as the Ex Parte 175 Method (T-652, Tables 7 through 12).

Confirmation of Mr. Bearss' belief in the relevancy, in rate cases, of rates of return computed on the ICC Elements of Value base is found in his recent submission to the Commission in *Utah Intrastate Freight Rates and Charges,* Doc. Nos. 31484 and 32253. He there submitted statistical data for four of the principal Transcontinental roads which included unadjusted and adjusted rates of return on the ICC Valuation base, with comment on the effects of leased equipment and time-lag in reporting capital expenditures, in addition to the book value base.

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[fol. 766] Use of the Elements of Value data, as well as Book Value data, in setting up a base for computing rate of return was included in Association of American Rail-

roads staff exhibits on behalf of the industry in one or more of the post-war general rate increase cases. Also, *Trends in Railroad Operations,* published by that Association in December, 1957, contains, in Table 8, a historical statement of the rate of return of the Class I Railways of the United States, 1925 to 1956, in which rate of return is shown "on net investment" and "on ICC Valuation", the latter conforming to the years in which the Commission's "Elements of Value" statements were available.

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[fol. 767] Substantial Advantage of Transcontinental Group In Earning Power and Rate of Return Shown Even in Mr. Bearss' Own Groupings

In Exhibit T-652 Mr. Bearss limited his direct "response" to the MW-608, 1951-56 average Book Value rate of return comparisons to comments regarding Table 44. On pages 12-13, he referred to the single instance in which his "Midwestern" groups, both "all roads" and "principal roads", were shown to have had an average fully adjusted rate of return nearly 2% greater than his Mountain-Pacific groups for 1951-1956. He made no reference to my Table 45 (year 1957) in which his Mountain-Pacific group's fully adjusted rate of return was shown to have been higher than his Midwestern groups—"all roads", in 1957; by 2.9%, and "principal roads" by 5.1%.

It may be noted further that these advantages of his Mountain-Pacific group's fully adjusted rate of return even on book value were further widened in 1958. On page 40

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[fol. 768] of Appendix A, Table 45a, of Exhibit MW-737 (JKL-3), it is shown that the 1958 advantage of Mr. Bearss' "All Roads" group was 13.0% and of his "Principal Roads" group was 12.0%.

These facts should be borne in mind in evaluating the following conclusion by Mr. Bearss, stated on page 13 of Exhibit T-652:

> "Witness Langum has already recognized the 'distortion' and 'abnormality' of unadjusted rates of return.

(MW-608, p. 31). But unadjusted or adjusted, his figures show the Mountain-Pacific carriers have experienced a lower rate of return than the Midwestern carriers. *It is only when he attempts to treat the Milwaukee as a completely Midwestern road, and when he goes further by excluding other Midwestern roads from his computation, that he is able to dilute the force of his own showing.*" (Emphasis supplied) (T-652, p. 13)

This statement is incorrect. In my sixteen tables of earning power and rate of return statistics *on Mr. Bearss' own groupings,* as shown above, there is only this one instance (MW-608, Table 44) in which the Bearss Mountain-Pacific group rate of return is shown to be less than that of his Midwestern group. In every one of my fifteen other tables containing measures of earning power and rate of return (MW-608, Tables 30 through 43 and Table 45), the very substantial advantage of Mr. Bearss' own groups of Mountain-Pacific roads over his groups of Midwestern roads is clearly evident.

Note should also be made of the improprieties of the inclusion by Mr. Bearss of the Milwaukee in his Mountain-Pacific group and the Transcontinental subsidiaries in the Midwestern-all roads group. Mr. Bearss avoided specific discussion of his Mountain-Pacific groups' still greater ad-

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[fol. 769] vantage when the Milwaukee was excluded therefrom and the Transcontinental subsidiaries were excluded from his Midwestern-all roads group. He simply referred to my alternate comparisons, quite erroneously, as "something by which I was "able to dilute the force of" my "own showing". On the contrary, in these alternate comparisons I emphasized the illogical character of the Bearss presentation.

Furthermore, in the comparisons throughout, the advantage of the Bearss Mountain-Pacific group over his Midwestern-all roads group is substantially widened by

evaluation of earning power and rate of return in terms of the ICC Valuation base.

My "own showing", in my analysis of Tables 30-45, demonstrated that "even in terms of Mr. Bearss' groupings, the higher level of earning power and rate of return of the Mountain-Pacific over the Midwestern railroads and the marked improvement during recent years in their favorable situation" was clearly apparent (MW-608, p. 98). In MW-608, on pages 131 to 137, the effect of the entire group of statistics in Tables 30-45 was correctly summarized. The much more advantageous position of Mr. Bearss' "own" Mountain-Pacific groups, both Class I and "principal roads", in the post-war period is there abundantly shown.

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[fol. 770] *Direct Railroad Operations versus Financial Position of Companies as a Whole*

In his comments in Exhibit T-659 (HJB-16), pages 1-3, 7-9, and 14-15, Mr. Bearss has brought confusion and misunderstanding into the sharp distinction which I made between two separate concepts.

On the one hand, the tables and testimony in Exhibit MW-608 from beginning to end dealt only with measurements of earning power and rate of return from direct railroad operations. In these studies the effects upon earning power and financial performance resulting from "other income" of the railroad companies did not enter in, in any manner.

On the other hand, the tables and testimony in Exhibit MW-609 gave "consideration . . . . primarily to further aspects of the financial testimony of several witnesses for the Transcontinental Railroads, viz: Messrs. Chandler, Bearss, Edwards, Gurley, Lovett, Russell, Macfarlane, Whitman, and Boles."

Inasmuch as Mr. Chandler in his Exhibits T-251 and T-252 and Mr. Bearss in Exhibit T-276 presented the results of specific studies of the financial position of the railroad companies in their so-called "Mountain-Pacific

Group", it was necessary in rebuttal to present the corresponding results of precisely identical studies of the financial position of the railroad companies in the Midwestern Group as compared with the financial position of the railroad companies in the Transcontinental Group.

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[fol. 771] Mr. Chandler's studies supplemented by those of Mr. Bearss, to which I responded in MW-609, were based primarily on measurements of appraisal by investors of securities and comparisons of the "Mountain-Pacific" railroads as business enterprises as a whole as compared with other business enterprises as a whole outside the railroad field. Mr. Chandler and Mr. Bearss manifestly believe that there is merit and relevancy in these proceedings in making comparisons of the Transcontinental railroads as business enterprises with other non-railroad business enterprises. Likewise, it appears to me as an economist that by the same token comparison of the Transcontinental railroads as business enterprises with the railroads in the Midwestern Group as business enterprises is every bit as meaningful and appropriate.

The sharp distinction and unequivocal position which I took and now take in regard to the separate aspects of earning power and rate of return from direct railroad operations, on the one hand, and the broader matters of credit standing, financial strength, and investor appraisal necessarily relating to the companies as a whole are clearly indicated in the following words from the section at the very end of Exhibit MW-609 which set forth the conclusions of my studies and testimony as a whole:

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[fol. 772] "In earning power and rate of return from direct railroad operations the Transcontinental Group stands far out ahead of the Midwestern Group. The Transcontinental Group's position as to credit rating and favor among investors is therefore much higher than that of the Midwestern Group. These attributes are enhanced by the relatively larger amount of income enjoyed by the majority of the principal Transcontinental roads from separately incorporated sub-

sidiary transportation operations and additional items classed as non-operating income. It is clear, however, that in terms alone of the data for direct railroad operations, the earnings performance and financial position of the Transcontinental Group is strikingly higher than that of the Midwestern Group."

"Considering earnings from direct railroad operations alone, the relatively much lower earnings of the Midwestern Group have left it in a position where it has fallen short of earning a fair return after payment of operating expenses and taxes to a greater extent than either of the other groups; and this is particularly true in comparison with the Transcontinental Group where the disparity is of large proportion. Furthermore, the continued trend has been toward greater improvement in earning power and financial condition in the other two groups in relation to the Midwestern Group."

"From my studies it is apparent that the Midwestern Group is in far greater need for additional revenue than the Transcontinental Group and moderately so in comparison with the Eastern Group."

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[fol. 773] *Bearss' Erroneous Concept of "Percentage of Funds Available from Transportation Operations"*

In a series of tables in Appendices G, H and I of Exhibit T-659 Mr. Bearss has carried through 1957 his concept of "Percentage of Funds Available From Transportation Operations".

My complete disagreement with this type of study, as having any relevant meaning in this proceeding, is set forth on pages 75 through 80 of Exhibit MW-609. What I there said applies as well to these more recent extensions of Exhibit T-275 statistics. For this reason, I have not undertaken further analysis of the Exhibit T-659, Appendices G, H and I tables. I do note, however, that Mr. Bearss in the table on page 4(a) of Appendix G introduced

an arbitrary weighting process and employed non-factual adjustments of C&NW and NYC statistics. These deviations merely extended his studies further into the realm of unreality. Nevertheless, in order to show the statistical effect of his groupings again, in comparison with the contestant groups, I caused a computation to be made for the principal roads in the latter groups, using the Book Value base and exactly the same steps as used in Appendix G, page 4(a) except that acquisition adjustment accounts were not deducted in our computation. The results were:

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[fol. 774]

Percentage of Funds Available From Transportation Operations To Net Investment In Property Used In Transportation Service
(So Termed By Mr. Bearss)

Bearss' Groupings (T-275)	*Percent*
Principal Mountain-Pacific Roads (7 Transcontinental Systems, plus Milwaukee)	1.18
Principal Midwestern Roads (4 Midwestern Contestants, plus CB&Q, StL-SW, T&NO and T&P)	1.58
Contestant Groups	
Principal Transcontinental (7 systems)	1.26
Principal Midwestern (10 systems)	1.00
Principal Midwestern, plus Milwaukee (11 systems)	.93

In Exhibit MW-609 I included Tables 10, 11 and 17, using as models the Chandler-Bearss Schedules 29, 30 and 32, and applying their methods and resultant operating and financial statistics, for purposes of comparison, to the prin-

cipal contestants in the Western District—i.e., Transcontinental (7 systems) and Midwestern (10 systems). In this exhibit I now include a reproduction of those tables to which have been added the corresponding statistics for the year 1958. These are designated as Tables 10a, 11a and 17a.

These added statistics in general show a continuation through 1958 of the relatively more advantageous position and trend of these Transcontinental roads.

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[fol. 775] Mr. Bearss, on page 17 of Exhibit T-659, listed North Western System operating and transportation ratios for years 1946 through 1958. He made no comparison with other roads, but made reference to Witness Boles' comment that the North Western's transportation ratio "was materially out of line with its other Midwestern neigh-

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[fol. 776] bors." He commented that the 1958 transportation and operating ratios were the lowest experienced in any post-war year,* evidently submitting this as support for his theory that North Western's statistics for past years should be excluded.

Without in the least conceding that such listings and comparisons of ratios could possibly justify exclusion of North Western's statistics, I wish to point out the very limited consideration Mr. Bearss has accorded this subject.

Attached hereto as Appendix B are reproductions of annual statistics which have been published by the Commission for the years 1950 through 1958 in which the operating ratios are separately stated for freight and passenger service of the large passenger-carrying roads. These include most of the principal railroads in each of the three contending groups. These tables are usually included in the May issue of "Monthly Comment on Transportation Statistics", presently entitled "Transport Economics".

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* The transportation ratio was 1.62 lower and the operating ratio .80 lower than the lowest previous year, 1947. (See Exhibit T-659, p. 17.)

Noting first the year by year passenger service operating ratio of the Chicago and North Western in comparison with the fifteen other Western District roads shown, it appears that its ratio has generally been in the middle area of magnitude among all of these large passenger-carrying roads. Its ratio was relatively somewhat above the majority during 1950, 1951, and 1952, although there were several roads having higher ratios during those years. Be-

[fol. 777] ginning in 1953 and extending through 1955, its ratio was definitely lower than the majority of the other roads, in 1955 there being only one other road, the Santa Fe, among the sixteen roads shown, which had a lower ratio. In 1956, 1957 and 1958, the roads having lower ratios numbered six, two and two, respectively.

In the column entitled "Percent passenger deficit of freight net railway operating income" in these tables, for the years 1954-1958, it is noted that, notwithstanding its average and less than average passenger service ratios throughout the years, the North Western has had the highest percent of freight net railway operating income required to offset the passenger deficit in every year since 1954. This reflects the relatively lesser amount of gross revenue from freight service which the North Western has been able to retain as net railway operating income, in comparison with these other large railroads in the Western District.

These Appendix B tables show that the North Western freight service operating ratio during the nine-year period was among the highest of the sixteen Western District roads shown. However, it was the highest in only one year, 1950. In each of the subsequent eight years there were at least three and more often five roads, in addition to the North Western, which had ratios in excess of 70.

Upon Mr. Bearss' theory, if operating ratios are the test, several other railroads are as likely candidates for exclusion as the North Western.

APPENDIX B

Large railways
(Dollar items in thousands)

Road	Net railway operating income				Operating ratios			
	Freight service		Passenger and allied services		Freight service		Passenger and allied services	
	1951	1950	1951	1950	1951	1950	1951	1950
			Deficit	Deficit				
Eastern district								
Baltimore & Ohio	$72,650	$65,070	$35,816	$30,927	72.04	71.72	172.84	166.99
Boston & Maine	19,937	19,154	15,030	12,201	58.96	56.75	167.29	149.09
D. L. & W.	13,601	13,195	5,111	4,147	72.02	69.49	121.62	115.39
Erie	31,720	29,702	11,971	10,236	67.57	65.52	172.05	161.62
Lehigh Valley	14,149	11,854	3,756	3,453	71.45	71.62	140.63	141.33
New York Central	93,878	71,070	54,266	33,966	75.10	74.92	118.11	108.66
N.Y., C. & St. L.	25,399	28,399	3,005	3,210	66.79	61.82	152.35	163.42
N.Y., N.H. & H.	19,808	20,269	11,918	9,368	67.19	62.68	98.90	97.04
Pennsylvania	131,047	92,507	71,688	34,845	75.56	77.29	121.95	107.94
Reading	22,068	21,489	8,793	8,532	71.17	69.96	172.40	180.24
Wabash	15,387	14,554	5,323	3,159	69.87	67.84	129.75	120.70
Pocahontas region								
Chesapeake & Ohio	63,654	58,221	14,212	12,342	66.47	64.73	169.57	161.80
Norfolk & Western	40,754	37,381	10,799	8,322	60.74	63.10	175.59	155.22
Southern region								
Atlantic Coast Line	19,259	16,244	9,222	6,427	71.05	71.59	121.62	114.97
Gulf, Mobile & Ohio	16,205	14,432	6,645	5,121	62.33	61.44	150.06	135.43
Illinois Central	43,565	47,255	12,907	9,586	68.74	65.99	127.26	117.94
Louisville & Nashville	41,551	38,947	17,211	12,915	67.51	65.60	150.61	139.75
Seaboard Air Line	29,303	24,572	10,118	7,211	63.74	63.00	133.97	121.30
Southern	42,094	42,382	14,147	10,449	64.56	61.93	126.64	120.44
Western district								
A. T. & S. F. and affiliated cos.	108,085	101,300	36,472	20,087	64.13	57.81	127.97	110.89
Chicago & N. W.	30,570	29,895	23,346	20,762	73.37	70.04	151.63	145.97
C. B. & Q.	46,099	47,705	15,988	9,904	61.48	57.61	126.98	111.01
C. M. St. P. & P.	39,227	43,479	23,901	21,539	71.96	67.49	150.24	145.08
C. R. I. & Pac.	30,676	30,880	13,419	10,945	65.46	62.23	128.14	123.66
D. & R. G. W.	15,929	14,430	4,217	4,485	60.01	62.98	160.97	156.32
Great Northern	41,741	42,729	18,527	15,296	64.48	61.76	158.29	143.59
M-K-T Lines	12,624	13,479	5,448	4,383	65.91	62.59	139.31	127.76
Missouri Pac.	35,368	39,411	11,406	7,751	74.32	67.14	128.07	116.32
Northern Pac.	28,686	33,113	12,355	10,424	70.46	65.07	162.08	150.13
St. L.-S. F.	20,630	22,501	7,987	6,935	69.46	65.35	142.65	139.77
St. L. S.W. Lines	10,941	13,306	2,246	2,130	57.08	53.71	198.52	192.35
Southern Pac. Co.	83,376	78,075	37,988	30,528	66.75	62.87	142.34	132.17
Texas & N. O.	17,924	18,175	6,745	5,198	68.37	66.53	128.27	125.22
Texas & Pacific	13,548	12,003	3,638	2,357	61.14	60.79	127.61	114.96
Union Pac. and leased lines	78,389	74,848	42,062	30,157	61.96	59.22	152.51	134.19

Large railways
(Dollar items in thousands)

Road	Net railway operating income				Operating ratios			
	Freight service		Passenger and allied services		Freight service		Passenger and allied services	
	1952	1951	1952	1951	1952	1951	1952	1951
			Deficit					
Eastern district								
Baltimore & Ohio	$79,987	$72,650	$35,647	$35,816	69.94	72.04	173.23	172.84
Boston & Maine	17,258	19,937	12,195	15,030	61.31	58.96	145.28	167.29
D. L. & W.	15,854	13,601	4,997	5,111	68.11	72.02	120.61	121.62
Erie	29,107	31,720	10,739	11,971	68.93	67.57	158.13	172.05
Lehigh Valley	14,939	14,149	4,009	3,756	70.44	71.45	145.12	140.63
New York Central	99,995	93,878	50,622	54,266	73.85	75.10	117.05	118.11
N.Y., C. & St. L.	25,048	25,399	2,282	3,005	65.74	66.79	140.00	152.35
N.Y., N.H. & H.	23,160	19,808	12,524	11,918	65.31	67.19	100.18	98.90
Pennsylvania	135,328	131,047	60,537	71,688	74.24	75.56	119.05	121.95
Reading	23,727	22,068	7,995	8,793	69.74	71.17	164.72	172.40
Wabash	18,002	14,571	4,385	4,508	67.82	69.87	132.20	129.75
Pocahontas region								
Chesapeake & Ohio	71,339	63,654	14,356	14,212	66.33	66.47	177.67	169.57
Norfolk & Western	38,970	40,754	10,422	10,799	64.35	60.74	177.60	175.59
Southern region								
Atlantic Coast Line	23,914	19,259	11,681	9,222	70.78	71.05	128.47	121.62
Gulf, Mobile & Ohio	16,789	16,205	6,154	6,645	61.44	62.33	150.02	150.06
Illinois Central	44,188	43,565	12,274	12,907	65.81	68.74	124.68	127.26
Louisville & Nashville	43,216	41,551	15,557	17,211	67.59	67.51	143.17	150.61
Seaboard Air Line	32,255	29,303	9,214	10,118	62.81	63.74	128.57	133.97
Southern	49,743	42,094	13,367	14,147	60.33	64.56	126.61	126.64
Western district								
A.T. & S.F. and affiliated cos.	100,287	108,085	30,913	36,472	59.66	64.13	120.75	127.97
Chicago & N. W.	30,649	30,570	22,521	23,346	72.33	73.37	148.10	151.63
C. B. & Q.	48,116	46,099	16,378	15,988	62.11	61.48	127.65	126.98
C., M., St. P. & P.	38,996	39,227	21,566	23,901	72.53	71.96	144.71	150.24
C.R.I. & Pac.	38,524	30,676	13,185	13,419	61.52	65.46	127.14	128.14
D. & R. G. W.	15,938	15,929	4,317	4,217	60.45	60.01	162.01	160.97
Great Northern	46,023	41,741	20,109	18,527	63.22	64.48	162.02	158.29
M-K-T Lines	16,485	12,624	5,744	5,448	62.92	65.91	147.87	139.31
Missouri Pacific	39,036	35,368	10,984	11,406	70.83	74.32	127.33	128.07
Northern Pacific	28,210	28,686	12,786	12,355	72.05	70.46	162.40	162.08
St. L. - S.F.	24,696	20,630	7,320	7,987	66.46	69.46	137.54	142.69
St. L. S. W. Lines	15,447	10,941	1,920	2,246	52.34	57.08	207.15	198.52
Southern Pac. Co.	95,155	83,376	37,052	37,988	64.75	66.75	138.08	142.34
Texas & N. O.	20,230	17,924	6,642	6,745	64.37	68.37	131.25	128.27
Texas & Pacific	17,420	13,548	4,091	3,638	58.68	61.14	132.00	127.61
Union Pac. and leased lines	74,999	78,389	41,717	42,062	62.84	61.96	148.44	152.51

[fol. 779]

Large railways, year 1953
(Dollar items in thousands)

Road	Net railway operating income		Operating ratios	
	Freight service	Passenger and allied services	Freight service	Passenger and allied services
		(Deficit)		
Eastern district				
Baltimore & Ohio	$80,535	$36,737	70.2	180.0
Boston & Maine	18,358	12,976	60.9	153.4
Central R.R. of New Jersey	14,133	9,243	63.8	185.9
Delaware, Lackawanna & Western	15,107	4,919	68.6	121.6
Erie	29,805	10,833	67.7	161.3
Lehigh Valley	14,362	3,827	71.8	142.9
Long Island	2,631	2,828	65.4	93.5
New York Central	114,656	52,439	71.8	119.2
New York Chicago & St. Louis	24,765	2,993	66.1	157.2
New York, New Haven & Hartford	23,327	13,368	65.1	102.6
Pennsylvania	131,332	56,650	74.4	118.8
Reading	24,852	7,986	70.1	165.5
Wabash	17,441	3,937	68.0	126.6
Pocahontas region				
Chesapeake & Ohio	75,037	15,121	67.0	179.4
Norfolk & Western	39,071	11,343	65.0	192.1
Southern region				
Atlantic Coast Line	27,342	17,045	72.4	146.5
Gulf, Mobile & Ohio	15,989	5,297	63.4	139.0
Illinois Central	46,422	13,482	64.1	128.5
Louisville & Nashville	49,437	15,052	64.1	144.1
Seaboard Air Line	34,151	10,322	61.2	134.9
Southern	56,703	14,717	58.4	134.1
Western district				
Atchison, Topeka & Santa Fe & Affl. Cos.	117,183	42,074	60.8	134.6
Chicago & North Western	32,377	23,420	71.1	152.8
Chicago, Burlington & Quincy	50,907	21,033	62.1	139.3
Chicago, Milwaukee, St. Paul & Pacific	36,568	21,904	74.0	150.3
Chicago, Rock Island & Pacific	42,611	14,352	59.4	131.5
Denver & Rio Grande Western	17,672	4,577	57.7	167.4
Great Northern	48,550	21,019	62.5	175.1
Missouri-Kansas-Texas Lines	15,635	6,150	64.1	150.5
Missouri Pacific	39,582	16,168	73.4	154.4
Northern Pacific	30,262	15,395	71.3	173.5
St. Louis-San Francisco	24,207	8,991	65.8	156.0
St. Louis Southwestern Lines	15,155	1,318	61.8	223.5
Southern Pacific Co.	93,032	45,919	66.0	153.8
Texas & New Orleans	17,423	5,209	65.8	125.5
Texas & Pacific	18,989	6,458	57.9	158.2
Union Pacific and leased lines	81,613	52,218	62.2	166.7

[fol. 780]

Large railways, year 1954
(Dollar items in thousands)

Road	Net railway operating income			Operating ratio	
	Freight service	Passenger and allied services (deficit)	Percent passenger deficit of freight net railway operating income	Freight service	Passenger and allied services
Eastern district					
Baltimore & Ohio	$61,312	$31,824	51.9	73.05	173.26
Boston & Maine	18,403	15,159	82.4	62.06	168.71
Central R. R. of New Jersey	10,745	6,998	65.1	65.46	161.39
Del., Lacka. & Western	11,123	4,052	36.4	74.97	116.61
Erie	21,726	9,070	41.7	74.71	153.40
Lehigh Valley	10,369	4,459	43.0	76.14	154.61
Long Island	1,764	3,664	207.7	68.87	96.22
New York Central	71,488	38,806	54.3	74.34	113.80
N. Y., C. & St. L.	21,619	2,954	13.7	68.15	163.90
N. Y., N. H. & H.	19,433	10,145	52.2	68.65	96.89
Pennsylvania	91,882	43,691	47.6	75.11	113.65
Reading	20,285	6,833	33.7	71.03	153.77
Wabash	16,263	4,126	25.4	72.03	128.33
Pocahontas region					
Chesapeake & Ohio	65,899	13,546	20.6	68.79	175.64
Norfolk & Western	37,331	11,254	30.1	66.58	204.93
Southern region					
Atlantic Coast Line	23,687	12,723	53.7	71.84	136.13
Gulf, Mobile & Ohio	14,150	5,227	36.9	66.67	146.75
Illinois Central	44,959	16,701	37.1	67.19	139.81
Louisville & Nashville	40,992	17,070	41.6	72.37	156.13
Seaboard Air Line	32,654	9,749	29.9	62.68	134.62
Southern	47,902	13,345	27.9	61.68	131.07
Western district					
A. T. and S. F. and affiliated companies	110,317	46,327	42.0	62.28	142.47
Chicago & North Western	21,173	20,521	96.9	74.96	146.48
Chicago, B. & Q.	48,776	21,032	43.1	63.86	140.66
C., M. St. P. & P.	37,393	22,825	61.0	72.91	157.50
Chic., R. I. & Pacific	36,333	15,579	42.9	63.71	137.22
Denver & R. G. W.	18,492	4,422	23.9	58.53	173.62
Great Northern	46,224	21,997	47.6	64.65	179.82
M-K-T Lines	13,460	6,303	46.8	67.33	159.84
Missouri Pacific	38,879	13,470	34.6	70.74	144.22
Northern Pacific	31,818	16,358	51.4	72.75	182.22
St. L.-San Francisco	20,446	9,280	45.4	71.12	164.98
St. L. S. W. Lines	9,835	1,139	11.6	61.18	195.84
Southern Pacific	93,282	51,141	54.8	67.89	169.10
Texas & New Orleans	12,904	6,866	53.2	72.05	142.08
Texas & Pacific	13,935	5,755	41.3	62.48	149.44
Union Pac. & Leased Lines	82,911	52,957	63.9	61.59	174.85

[fol. 781]

Large Railroads, year 1955
(Dollar items in thousands)

Road	Net railway operating income			Operating ratio	
	Freight service	Passenger and allied services (deficit)	Percent passenger deficit of freight net railway operating income	Freight service	Passenger and allied services
Eastern district					
Baltimore & Ohio	$71,534	$32,635	45.6	72.78	180.77
Boston & Maine	19,145	12,250	64.0	56.80	156.42
Central R. R. of New Jersey	11,302	6,736	59.6	65.90	160.36
Del., Lacka. & Western	7,451	4,822	64.7	77.94	122.86
Erie	24,560	9,545	38.9	72.37	159.79
Lehigh Valley	12,599	4,345	34.5	74.80	159.20
Long Island	1,196	cr. 205	-	72.04	89.41
New York Central	111,282	37,788	34.0	69.32	114.02
N. Y., C. & St. L.	25,238	3,365	13.3	65.54	180.66
N. Y., N. H. & H.	19,988	14,165	70.9	65.36	105.90
Pennsylvania	119,013	49,976	42.0	73.30	117.82
Reading	21,921	6,830	31.2	69.72	161.14
Wabash	21,131	3,566	16.9	68.99	121.21
Pocahontas region					
Chesapeake & Ohio	80,891	11,982	14.8	64.06	165.89
Norfolk & Western	48,806	10,965	22.5	60.21	213.47
Southern region					
Atlantic Coast Line	25,615	12,712	49.6	72.25	138.70
Gulf, Mobile & Ohio	14,486	4,655	32.1	66.19	140.58
Illinois Central	46,441	14,212	30.6	64.71	129.98
Louisville & Nashville	42,091	13,076	31.1	69.40	154.89
Seaboard Air Line	34,241	9,878	28.8	61.96	134.31
Southern	63,695	15,265	24.0	56.40	138.29
Western district					
A. T. and S. F. and affiliated companies	114,631	40,858	35.6	60.85	136.33
Chicago & North Western	25,998	18,331	70.5	72.42	141.10
Chicago, B. & Q.	48,181	21,695	45.0	65.04	143.40
C., M. St. P. & P.	37,054	21,274	57.4	73.56	155.84
Chic., R. I. & Pacific	37,918	16,938	44.7	63.08	142.96
Denver & R. G. W.	19,569	4,615	23.6	54.40	177.92
Great Northern	52,167	22,012	42.2	62.67	181.32
M-K-T Lines	12,876	6,515	50.6	68.60	169.28
Missouri Pacific	40,223	12,720	31.6	70.49	142.41
Northern Pacific	34,612	15,388	44.5	69.04	181.60
St. L.-San Francisco	23,139	8,924	38.6	68.20	164.68
St. L. S. W. Lines	11,954	1,268	10.6	56.69	214.87
Southern Pacific	92,979	43,450	46.7	69.72	161.94
Texas & New Orleans	14,546	6,785	46.6	71.41	149.13
Texas & Pacific	15,765	5,611	35.6	61.65	149.74
Union Pac. & Leased Lines	90,334	46,223	51.2	60.33	166.57

[fol. 782]

Large Railroads, year 1956
(Dollar items in thousands)

Road	Net railway operating income			Operating ratio	
	Freight service	Passenger and allied services (deficit)	Percent passenger deficit of freight net railway operating income	Freight service	Passenger and allied services
Eastern district					
Baltimore & Ohio	$77,247	$33,789	43.7	72.73	183.52
Boston & Maine	18,437	13,679	74.2	60.31	162.07
Central R. R. of New Jersey	11,569	7,018	60.7	65.94	159.64
Del., Lacka, & Western	13,415	5,251	39.1	74.90	122.74
Erie	25,720	10,445	40.6	71.40	161.67
Lehigh Valley	11,218	4,492	40.0	75.16	167.61
Long Island	958	cr. 940	-	74.28	89.50
New York Central	106,472	48,476	45.5	70.69	119.39
N. Y., C. & St. L.	25,737	4,104	15.9	67.24	201.16
N. Y., N. H. & H.	17,394	14,834	85.3	66.05	102.22
Pennsylvania	121,832	54,683	44.9	73.76	118.89
Reading	24,179	7,968	33.0	69.40	166.41
Wabash	17,196	5,096	29.6	70.64	132.28
Pocahontas region					
Chesapeake & Ohio	89,656	12,084	13.5	64.33	166.50
Norfolk & Western	52,648	11,332	21.5	63.50	221.33
Southern region					
Atlantic Coast Line	21,962	12,694	57.8	75.25	135.49
Gulf, Mobile & Ohio	13,333	5,809	43.6	67.26	156.18
Illinois Central	46,819	18,809	40.2	65.83	143.68
Louisville & Nashville	43,041	15,683	36.4	70.73	157.56
Seaboard Air Line	32,479	9,541	29.4	64.69	130.88
Southern	62,870	17,179	27.3	59.44	144.93
Western district					
A. T. and S. F. and affiliated companies	117,811	52,479	44.5	63.59	146.55
Chicago & North Western	20,820	19,888	95.5	76.19	156.14
Chicago, B. & Q.	49,626	24,090	48.5	64.29	145.36
C., M. St. P. & P.	40,680	23,335	57.4	72.41	153.21
Chic., R. I. & Pacific	38,064	17,683	46.5	64.65	145.15
Denver & R. G. W.	20,445	4,951	24.2	55.60	182.63
Great Northern	54,373	23,966	44.1	64.61	193.86
M-K-T Lines	11,864	6,540	55.1	70.32	170.31
Missouri Pacific	57,736	18,412	31.9	68.72	149.48
Northern Pacific	33,514	15,639	46.7	71.16	186.07
St. L.-San Francisco	23,486	9,285	39.5	70.17	169.29
St. L. S. W. Lines	11,774	875	7.4	61.02	194.59
Southern Pacific	91,179	49,953	54.8	71.03	173.08
Texas & New Orleans	12,833	5,286	41.2	72.84	137.81
Texas & Pacific	15,456	6,123	39.6	65.42	152.44
Union Pac. & Leased Lines	85,504	42,956	50.2	61.76	163.51

[fol. 783]

Large Railroads, year 1957
(Dollar items in thousands)

Road	Net railway operating income			Operating ratio	
	Freight service	Passenger and allied services (deficit)	Percent passenger deficit of freight net railway operating income	Freight service	Passenger and allied services
Eastern district					
Baltimore & Ohio	$71,959	$34,041	47.3	73.00	186.87
Boston & Maine	18,109	12,590	69.5	60.90	159.91
Central R. R. of New Jersey	10,437	7,054	67.6	66.84	156.34
Del., Lacka. & Western	8,995	5,543	61.6	76.21	130.06
Erie	23,164	12,375	53.4	73.89	180.43
Lehigh Valley	5,723	4,777	83.5	80.53	174.41
Long Island	1,137	dr. 982	-	73.33	89.88
New York Central	81,685	52,283	64.0	74.07	125.18
N. Y., C. & St. L.	23,689	3,997	16.9	69.03	198.16
N. Y., N. H. & H.	15,618	15,225	97.5	68.35	101.73
Pennsylvania	100,788	57,531	57.1	76.67	120.52
Reading	25,451	9,047	35.5	72.19	178.64
Wabash	17,098	6,117	35.8	72.40	143.21
Pocahontas region					
Chesapeake & Ohio	92,987	14,832	16.0	65.42	185.26
Norfolk & Western	56,342	11,666	20.7	63.06	235.91
Southern region					
Atlantic Coast Line	22,397	13,191	58.9	73.31	138.20
Gulf, Mobile & Ohio	10,903	5,817	53.4	71.76	158.37
Illinois Central	40,847	20,014	49.0	70.06	146.60
Louisville & Nashville	41,703	18,340	44.0	74.39	168.17
Seaboard Air Line	32,227	10,884	33.8	65.13	136.00
Southern	59,465	18,934	31.8	61.75	152.88
Western district					
A. T. and S. F. and affiliated companies	109,568	53,258	48.6	66.16	149.72
Chicago & North Western	25,047	19,591	78.2	74.70	148.90
Chicago, B. & Q.	45,733	24,738	54.1	67.63	146.41
C., M. St. P. & P.	40,614	24,195	59.6	71.00	161.64
Chic., R. I. & Pacific	34,871	20,547	58.9	65.99	155.44
Denver & R. G. W.	21,425	5,451	25.4	56.04	193.04
Great Northern	51,005	26,151	51.3	66.32	202.00
M-K-T Lines	7,664	5,374	70.1	73.16	165.41
Missouri Pacific	53,482	17,726	33.1	69.30	149.67
Northern Pacific	34,950	17,549	50.2	72.44	199.17
St. L-San Francisco	21,060	9,795	46.5	72.81	178.65
St. L. S. W. Lines	10,580	854	8.1	63.06	221.41
Southern Pacific	92,346	47,316	51.2	71.33	174.10
Texas & New Orleans	12,767	3,962	31.0	71.00	126.85
Texas & Pacific	12,580	6,300	50.1	65.32	154.45
Union Pac. & Leased Lines	82,881	43,585	52.6	62.77	166.65

[fol. 784]

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Large Railroads, year 1958
(Dollar items in thousands)

Road	Net railway operating income			Operating ratio	
	Freight service	Passenger and allied services (deficit)	Percent passenger deficit of freight net railway operating income	Freight service	Passenger and allied services
Eastern district					
Baltimore & Ohio	$53,936	$25,347	47.0	73.50	169.61
Boston & Maine	11,550	9,636	83.4	65.96	147.83
Central R. R. of New Jersey	8,130	7,798	95.9	68.76	166.78
Del., Lacka. & Western	2,421	3,894	160.8	82.88	114.30
Erie	12,087	9,451	78.2	77.42	143.54
Lehigh Valley	739	4,100	554.8	85.04	163.43
Long Island	120	cr 1,692	-	81.15	89.07
New York Central	44,157	32,561	73.7	77.16	112.24
N. Y., C. & St. L.	18,988	3,540	18.6	70.37	171.93
N.Y., N. H. & H.	7,129	10,878	152.6	73.95	95.57
Pennsylvania	56,324	44,356	78.8	76.87	113.35
Reading	16,585	7,326	44.2	75.90	167.08
Wabash	12,820	7,058	55.1	75.20	156.00
Pocahontas region					
Chesapeake & Ohio	74,975	11,535	15.4	67.79	158.20
Norfolk & Western	53,240	9,430	17.7	60.55	186.31
Southern region					
Atlantic Coast Line	17,831	9,204	51.6	74.19	126.99
Gulf, Mobile & Ohio	10,207	4,522	44.3	72.70	150.78
Illinois Central	41,437	18,141	43.8	69.22	142.78
Louisville & Nashville	36,158	17,337	47.9	74.62	163.36
Seaboard Air Line	30,447	12,041	39.5	68.93	142.35
Southern	54,971	17,495	31.8	63.05	155.09
Western district					
A. T. and S. F. and affiliated companies	103,432	40,150	38.8	64.78	136.33
Chicago & North Western	24,853	15,992	64.3	73.80	140.57
Chicago, B. & Q.	47,356	23,691	50.0	65.92	144.23
C., M. St. P. & P.	40,411	23,540	58.3	70.71	163.73
Chic., R. I. & Pacific	32,109	18,920	58.9	66.38	150.95
Denver & R. G. W.	18,364	5,098	27.8	57.23	186.89
Great Northern	49,632	23,809	48.0	64.93	191.30
M-K-T Lines	7,914	3,476	43.9	68.38	153.77
Missouri Pacific	52,067	17,839	34.3	69.08	150.87
Northern Pacific	35,047	16,822	48.0	69.50	200.11
St. L-San Francisco	20,435	8,702	42.6	73.32	179.00
St. L. S. W. Lines	9,630	671	7.0	65.58	265.21
Southern Pacific	84,088	40,567	48.2	72.07	163.67
Texas & New Orleans	9,305	1,901	20.4	73.39	108.35
Texas & Pacific	10,077	5,312	52.7	70.35	146
Union Pac. & Leased Lines	87,854	43,954	50.0	61.94	16[illegible]

[fol. 785]

[fol. 786]

BEFORE THE
INTERSTATE COMMERCE COMMISSION

Exhibit MW-773 Revised (WEC-62)
Witness: Wm. E. Carpenter

Docket No. 31503 and Sub Numbers
TRANSCONTINENTAL DIVISIONS

Cost Scales
on
Various Bases

Pro No. 59-E-25

—2—

[fol. 787] *Development of Various Cost Bases*

The cost percentages on several bases are shown in Table 2 for the Edwards "Official" sample, i.e., traffic moving between Official and Mountain Pacific territories. For the Midwest sample of Witness Edwards, i.e., traffic moving between Midwest and Transcontinental territories, the cost percentages are shown in Table 3.

Table 2 has on line 3, column (a), for Basis A-1, a total figure in the amount of $15,065,486. This is the same figure as that used in my Exhibit MW-768 (WEC-57), page 3, column (a). As I said in that exhibit, this is the figure from which we started in our measurement of Witness Edwards' special adjustments. It reflects the corrections which we made in his original data, and it excludes the special services costs. The amounts and percentages shown for the various groups of railroads differ between these two exhibits, since Exhibit MW-768 (WEC-57) reflects Witness Edwards' "revenue" grouping of the roads as used by him in Appendix C of Exhibit T-632, and this exhibit reflects his "cost" grouping of the roads in his Appendix E of T-632.

Table 2
Official - Mountain Pacific Traffic
Percentages of Total Cost
Various Bases
Edwards' T-632 Appendix E Railroad Groups
1953 Traffic Units - 1956 Service Unit Costs

Line No.	Item	Total (a)	Official (b)	Midwest (c)	T.C. (d)
	A-1. FKE aggregates, corrected, excluding special services				
1	Line-haul		$3,084,519	$4,128,633	$6,519,747
2	Terminal		521,801	303	810,483
3	Total	$15,065,486	3,606,320	4,128,936	7,330,230
4	Percents	100.00	23.94	27.41	48.65
	B. FKE aggregates, corrected, excluding special services & Edwards' detailed adjustments				
5	Line-haul		3,590,017	5,074,533	6,394,007
6	Terminal		559,019	317	644,418
7	Total	16,262,311	4,149,036	5,074,850	7,038,425
8	Percents	100.00	25.51	31.21	43.28
	C. FKE aggregates, corrected, excluding special services & Edwards' detailed adjustments. Seven-day study empty-return ratios substituted for Edwards' empty-return ratios.				
9	Line-haul		3,909,746	5,314,955	6,193,458
10	Terminal		559,019	317	644,418
11	Total	16,621,913	4,468,765	5,315,272	6,837,876
12	Percents	100.00	26.88	31.98	41.14
	D. FKE aggregates, corrected, excluding special services & Edwards' detailed adjustments. Seven-day study empty-return ratios substituted for Edwards' empty-return ratios. Return on value calculated at 4 percent on I.C.C. elements-of-value rate base.				
13	Line-haul		3,624,532	4,892,878	5,599,324
14	Terminal		520,353	304	581,748
15	Total	15,219,139	4,144,885	4,893,182	6,181,072
16	Percents	100.00	27.23	32.15	40.62

Table 3
Midwest - Transcontinental Traffic
Percentages of Total Cost
Various Bases
Edwards' T-632 Appendix E Railroad Groups
1953 Traffic Units - 1956 Service Unit Costs

Line No.	Item	Total (a)	Midwest (b)	T.C. (c)
	A. FKE aggregates, corrected, excluding special services			
1	Line-haul		$3,405,338	$5,885,886
2	Terminal		500,104	671,598
3	Total	$10,462,926	3,905,442	6,557,484
4	Percents	100.00	37.33	62.67
	B. FKE aggregates, corrected, excluding special services & Edwards' detailed adjustments			
5	Line-haul		4,030,689	5,772,443
6	Terminal		487,956	581,783
7	Total	10,872,871	4,518,645	6,354,226
8	Percents	100.00	41.56	58.44
	C. FKE aggregates, corrected, excluding special services & Edwards' detailed adjustments. Seven-day study empty-return ratios substituted for Edwards' empty-return ratios.			
9	Line-haul		4,291,031	5,754,687
10	Terminal		487,956	581,783
11	Total	11,115,457	4,778,987	6,336,470
12	Percents	100.00	42.99	57.01
	D. FKE aggregates, corrected, excluding special services & Edwards' detailed adjustments. Seven-day study empty-return ratios substituted for Edwards' empty-return ratios. Return on value calculated at 4 percent on I.C.C. elements-of-value rate base.			
13	Line-haul		3,945,590	5,181,751
14	Terminal		458,843	522,109
15	Total	10,108,293	4,404,433	5,703,860
16	Percents	100.00	43.57	56.43

[fol. 789]

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[fol. 790] Basis B on Table 2 has a total figure shown on line 7, column (a), of $16,262,311. This is the same money as shown in my Exhibit MW-768 (WEC-57), on page 5, line 77, column (a). The difference between the figures shown in that exhibit of $16,262,305 and the figure on line 7 of Table 2 of this exhibit, amounting to $6, is due to "rounding".

Basis C on Table 2 includes (1) all the adjustments represented in the data shown for Basis B, and in addition, (2) the substitution of the Cost Section's seven-day study empty-return ratios for the return ratios used by Witness Edwards in his costing. His empty-return ratios appear in his Exhibit T-632, Appendix B, Section B. The empty-return ratios which were substituted to develop Basis C represent the experience of the groups of railroads in the cost districts, as Witness Edwards used them. For the "split" roads, system figures were used for both "sectors."

Basis D on Table 2 includes (1) all of the adjustments contained in Basis B, (2) the substitution of the seven-day study empty-return ratios contained in Basis C, and, in addition, (3) the return on value at four percent on elements of value, rather than six percent on net investment, as Witness Edwards used it.

Basis D represents, as nearly as we have been able to compute it, the cost amounts and the cost percentages which would be obtained by the use of Rail Form A system-average costs. This is the kind of Rail Form A cost which I used in my waybill costing, Exhibit MW-766 (WEC-55).

Table 3 is set up in the same fashion as Table 2 and deals with the Midwest-Transcontinental portion of the Edwards traffic and cost study. The calculations made in Table 3 are of the same nature as I described for Table 2. The bases in Table 3 represent the same adjustments in Witness Edwards' cost as do the bases in Table 2.

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[fol. 791] *Cost Scales*

In Appendix A of this exhibit, I show nine different cost scales, pages 1 through 9. In Appendix B I show the termi-

nal and line-haul costs associated with each of these nine scales.

On page 1 of Appendix A, the scales shown represent the out-of-pocket Rail Form A costs applied to the Commission's waybill traffic for the years 1953, 1954 and 1955. These costs represent those for the average-weight train. The nature of these costs and the results of the application of them to the waybill traffic is set forth in detail in my Exhibit MW-766 (WEC-55).

The scales shown on page 2 of Appendix A represent the same traffic and cost as those on page 1 except that here the costs are on a fully distributed basis rather than the out-of-pocket basis used on page 1.

The cost scales on page 3 of Appendix A are on an out-of-pocket basis. They differ from those on page 1 in that they reflect the way-train miles in the various areas as Witness Edwards "traced" them. The way-train miles which were used are shown at the foot of the cost scale.

The scales on page 4 of Appendix A are constructed in the same fashion as those on page 3 except that the costs on page 4 are on the fully distributed level.

On page 5 of Appendix A the scales shown are at the out-of-pocket level. The way-train costs computed for the various groups reflect the Cost Section's original seven-day study.

The scales shown on page 6 of Appendix A are constructed in the same fashion as those on page 5. Those on page 6, however, are at the fully distributed level.

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[fol. 792] On page 7, Appendix A, the scales which are shown represent Witness Edwards' traffic and are based on average-train costs. The costs used for line-haul and terminal, which appear on page 7 of Appendix B of this exhibit are the same costs shown on Tables 2 and 3 of this exhibit, on lines 13 and 14. They represent the Basis D costs on those tables.

The cost scales shown on page 8 of Appendix A are for the same traffic and are on the same basis as those on page

7 except that the way-train costs and through-train costs for each railroad group were developed in aggregate on the Rail Form A Footnote 5 basis. These aggregate way-train costs and aggregate through-train costs were then combined, and the sum of the two was used in arriving at line-haul costs per hundredweight-mile for each railroad group. This method applies to each hundredweight-mile a portion of the way-train costs. This method differs from that of Witness Edwards in that his way-train costs are all at one end of the scale.

The scales on page 9 of Appendix A represent the same traffic and costs as those on pages 7 and 8, except that here, the way-train costs and the through-train costs were developed on the basis of Witness Edwards' Table 12 method. As on page 8, these way-train costs and through-train costs were aggregated and combined in arriving at the cost per hundredweight-mile for the line-haul portion of the costs.

Edwards' Basis D Costs in Cents per Hundredweight
Incurred in Handling Transcontinental Traffic
Edwards' Exhibit T-632 Traffic
Average Weight Trains

	Official-Mountain Pacific			Midwest-Transcontinental	
Miles	Mt.Pac. (a)	Midwest (b)	Official (c)	Mt.Pac. (d)	Midwest (e)
100	9.84	4.34	10.32	9.23	8.56
200	14.30	8.68	15.83	13.30	12.58
300	18.76	13.02	21.34	17.37	16.60
400	23.22	17.36	26.85	21.44	20.62
500	27.68	21.70	32.36	25.51	24.64
600	32.14	26.04	37.87	29.58	28.66
700	36.60	30.38	43.38	33.65	32.68
800	41.06	34.72	48.89	37.72	36.70
900	45.52	39.06	54.40	41.79	40.72
1000	49.98	43.40	59.91	45.86	44.74
1100	54.44	47.74	63.42	49.93	48.76
1200	58.90	52.08	70.93	54.00	52.78
1300	63.36	56.42	76.44	58.07	56.80
1400	67.82	60.76	81.95	62.14	60.82
1500	72.28	65.10	87.46	66.21	64.84
1600	76.74	69.44	92.97	70.28	68.86
1700	81.20	73.78	98.48	74.35	72.88
1800	85.66	78.12	103.99	78.42	76.90
1900	90.12	82.46	109.50	82.49	80.92
2000	94.58	86.80	115.01	86.56	84.94

Edwards' Basis D Costs in Cents per Hundredweight
Incurred in Handling Transcontinental Traffic
Edwards' Exhibit T-632 Traffic
Edwards' Way-Train Miles*

	Official-Mountain Pacific			Midwest-Transcontinental	
Miles	Mt.Pac. (a)	Midwest (b)	Official (c)	Mt.Pac. (d)	Midwest (e)
100	9.75	4.20	10.22	9.15	8.44
200	14.13	8.39	15.63	13.14	12.35
300	18.50	12.59	21.03	17.12	16.25
400	22.88	16.78	26.44	21.11	20.15
500	27.26	20.97	31.85	25.09	24.05
600	31.63	25.17	37.26	29.08	27.96
700	36.01	29.36	42.67	33.06	31.86
800	40.38	33.56	48.07	37.05	35.76
900	44.76	37.75	53.48	41.03	39.67
1000	49.14	41.94	58.89	45.02	43.57
1100	53.51	46.14	64.30	49.00	47.47
1200	57.89	50.33	69.71	52.99	51.38
1300	62.26	54.53	75.11	56.97	55.28
1400	66.64	58.72	80.52	60.96	59.18
1500	71.02	62.91	85.93	64.94	63.08
1600	75.39	67.11	91.34	68.93	66.99
1700	79.77	71.30	96.75	72.91	70.89
1800	84.14	75.50	102.15	76.90	74.79
1900	88.52	79.69	107.56	80.88	78.70
2000	92.90	83.88	112.97	84.87	82.60

* Way-train - through-train separations on Footnote 5 basis.

N.B.: Way-train miles:

33.0	--	9.0	30.6	10.1

[fol. 794]

Edwards' Basis D Costs in Cents per Hundredweight
Incurred in Handling Transcontinental Traffic
Edwards' Exhibit T-632 Traffic
Edwards' Way-Train Miles*

	Official-Mountain Pacific			Midwest-Transcontinental	
Miles	Mt.Pac. (a)	Midwest (b)	Official (c)	Mt.Pac. (d)	Midwest (e)
100	9.77	4.24	10.25	9.17	8.48
200	14.17	8.47	15.70	13.18	12.41
300	18.57	12.70	21.14	17.19	16.35
400	22.96	16.93	26.59	21.19	20.28
500	27.36	21.16	32.03	25.20	24.22
600	31.76	25.40	37.47	29.21	28.16
700	36.16	29.63	42.92	33.21	32.09
800	40.55	33.86	48.36	37.22	36.03
900	44.95	38.09	53.81	41.23	39.96
1000	49.35	42.32	59.25	45.24	43.90
1100	53.74	46.56	64.69	49.24	47.84
1200	58.14	50.79	70.14	53.25	51.77
1300	62.54	55.02	75.58	57.26	55.71
1400	66.93	59.25	81.03	61.26	59.64
1500	71.33	63.48	86.47	65.27	63.58
1600	75.73	67.72	91.91	69.28	67.52
1700	80.13	71.95	97.36	73.28	71.45
1800	84.52	76.18	102.80	77.29	75.39
1900	88.92	80.41	108.25	81.30	79.32
2000	93.32	84.64	113.69	85.31	83.26

* Way-train - through-train separations on Table 12 basis.

N.B.: Way-train miles:

33.0	--	9.0	30.6	10.1

[fol. 795]

SEPARATION OF LINE-HAUL COSTS SHOWN ON PAGE 8 APPENDIX B, EXHIBIT NO. MW-773, BETWEEN WAY TRAINS AND THROUGH TRAINS, AS REQUESTED BY MR. ESHELMAN AT TRANSCRIPT PAGE NO. 10796

(The terminal and line-haul costs shown are on "Basis D," as explained on page 3, Exhibit MW-773, applied to the transcontinental traffic covered by Edwards' Exhibit T-632 and reflect Edwards' way-train miles.)

Line No.	Item	Official-Mountain Pacific M.P. (a)	M.W. (b)	Off. (c)	Midwest-Transcontinental M.P. (d)	M.W. (e)
	Terminal					
1	Dollars	581,748	304	520,353	522,109	458,843
2	Hundredweight	10,820,500	10,820,500	10,820,500	10,109,240	10,109,240
3	Cost per Cwt. (Cents)	5.376	.003	4.809	5.165	4.539
	Line-Haul - Not Separated					
4	Dollars	5,495,555	4,729,816	3,556,145	5,071,632	3,826,901
5	Cwt.-miles (000)	12,557,523	11,283,137	6,574,782	12,729,711	9,809,013
6	Cost per Cwt.-Mile (Cents)	.04376	.04192	.05409	.03984	.03901
	Line-Haul - Separated on Footnote 5 Basis					
	Way Trains					
7	Dollars	241,278	5,576	64,161	185,409	56,405
8	Cwt.-Miles (000)	414,495	11,672	111,051	348,620	121,888
9	Cost per Cwt.-Mile (Cents)	.05821	.04777	.05778	.05318	.04628
	Through Trains					
10	Dollars	5,254,277	4,724,240	3,491,984	4,886,223	3,770,496
11	Cwt.-Miles (000)	12,143,028	11,271,465	6,463,731	12,381,091	9,687,125
12	Cost per Cwt.-Mile (Cents)	.04327	.04191	.05402	.03947	.03892

SEPARATION OF LINE-HAUL COSTS SHOWN ON PAGE 9 APPENDIX B, EXHIBIT NO. MW-773, BETWEEN WAY TRAINS AND THROUGH TRAINS, AS REQUESTED BY MR. ESHELMAN AT TRANSCRIPT PAGE NO. 10796

(The terminal and line-haul costs shown are on "Basis D," as explained on page 3, Exhibit MW-773, applied to the transcontinental traffic covered by Edwards' Exhibit T-632 and reflect Edwards' way-train miles.)

Line No.	Item	Official-Mountain Pacific M.P. (a)	M.W. (b)	Off. (c)	Midwest-Transcontinental M.P. (d)	M.W. (e)
	Terminal					
1	Dollars	581,748	304	520,353	522,109	458,843
2	Hundredweight	10,820,500	10,820,500	10,820,500	10,109,240	10,109,240
3	Cost per Cwt. (Cents)	5.376	.003	4.809	5.165	4.539
	Line-Haul - Not Separated					
4	Dollars	5,522,823	4,772,755	3,580,601	5,100,149	3,858,360
5	Cwt.-miles (000)	12,557,523	11,283,137	6,574,782	12,729,711	9,809,013
6	Cost per Cwt.-Mile (Cents)	.04398	.04230	.05446	.04006	.03933
	Line-Haul - Separated on Table 12 Basis					
	Way Trains					
7	Dollars	224,612	5,229	58,724	172,355	52,872
8	Cwt.-Miles (000)	414,495	11,672	111,051	348,620	121,888
9	Cost per Cwt.-Mile (Cents)	.05419	.04480	.05288	.04944	.04338
	Through Trains					
10	Dollars	5,298,211	4,767,526	3,521,877	4,927,794	3,805,488
11	Cwt.-Miles (000)	12,143,028	11,271,465	6,463,731	12,381,091	9,687,125
12	Cost per Cwt.-Mile (Cents)	.04363	.04230	.05449	.03980	.03928

[fol. 798]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Transcontinental Divisions Cases.

No. 31503 and Sub Nos.

THE AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY et al.

vs.

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY et al.

BRIEF OF MOUNTAIN-PACIFIC RAILROADS.—Filed June 13, 1960

S. R. Brittingham, Jr., R. Granville Curry, Frank S. Farrell, Lawrence W. Hobbs, Thormund A. Miller, Ernest Porter, Howard V. Rhedin, L. E. Torinus, Jr., E. L. Van Dellen, Howard J. Trienens, Douglas F. Smith, Counsel for the Mountain-Pacific Railroads.

Due Date: June 13, 1960.

* * * * * * *

[fol. 799]

B. The Docket 29886 and Docket 28277 Divisional Integer Scales, Based on Rate Scales, Would Produce Grossly Unfair and Confiscatory Divisions for the Long Haul Carriers of Transcontinental Traffic.

The divisional integer scales initially proposed by the Eastern lines and presently urged by the Midwestern roads [fol. 800] are derived from and strongly reflect the construction of rate scales which have a depressed progression, or taper, designed to facilitate the movement of long haul traffic. This characteristic of a rate scale, which has no bearing whatever upon the relative contribution of the carriers to the joint service, severely and unfairly depresses the divisions of the long haul carrier if a rate scale is used as the basis for constructing divisional scales. Application of such scales to the transcontinental traffic would be inherently confiscatory to the long haul Mountain-Pacific lines.

1. The Use of Divisional Integer Scales.

The operation of divisional integer scales may be illustrated by the following examples. For purpose of illustration, these examples assume that only two carriers are involved and that each road has the cost characteristics of the United States average railroad.

The scales set forth below are drawn from: (1) the scale prescribed in Docket 29886, *Official-Southwestern Divisions*, 287 I. C. C. 553, 595 (column 1); (2) the scale prescribed in Docket 28277, *Official Western Trunk Line Divisions*, 269 I. C. C. 765, 788 (column 1); and, for comparative purposes, (3) the United States average costs, as shown by Rail Form A:

Miles	(1) Docket 29886* Scale	(2) Docket 28277* Scale	(3) U. S. Average Cost** Scale
50	65	42	9.584
100	77	52	13.137
200	101	72	20.243
300	125	92	27.349
400	149	107	34.455
500	174	122	41.561
600	198	137	48.667
1000	294	195	77.091
1500	415	260	112.621
2000	535	316	148.151

An integer scale is employed to obtain percentage divisions in the following manner: If carrier A has a haul of 500 miles, its factor under the Docket 29886 scale would be 174; carrier B with a haul of 600 miles would have a factor [fol. 801] of 198. The sum of 174 and 198 is 372. Carrier A's percentage division would be 174 divided by 372, or 46.8%; carrier B's division would be 198 divided by 372, or 53.2% of the through revenue.

Applying each of the scales produces the following comparisons where the hauls are 500 and 600 miles, respectively:

	Docket 29886 Scale	Docket 28277 Scale	U. S. Average Cost Scale
Carrier A (500 miles)	46.8%	47.1%	46.1%
Carrier B (600 miles)	53.2%	52.9%	53.9%

* The scale prescribed in Docket 29886 ended with 1600 miles and the scale prescribed in Docket 28277 ended with 1200 miles. The Eastern and Midwestern lines have extended the scales on the same basis as the integers prescribed (Exhibit E-56; Exhibit T-299, Appx. A).

** Exhibit T-300, Appendix B, p. 1 (one terminal).

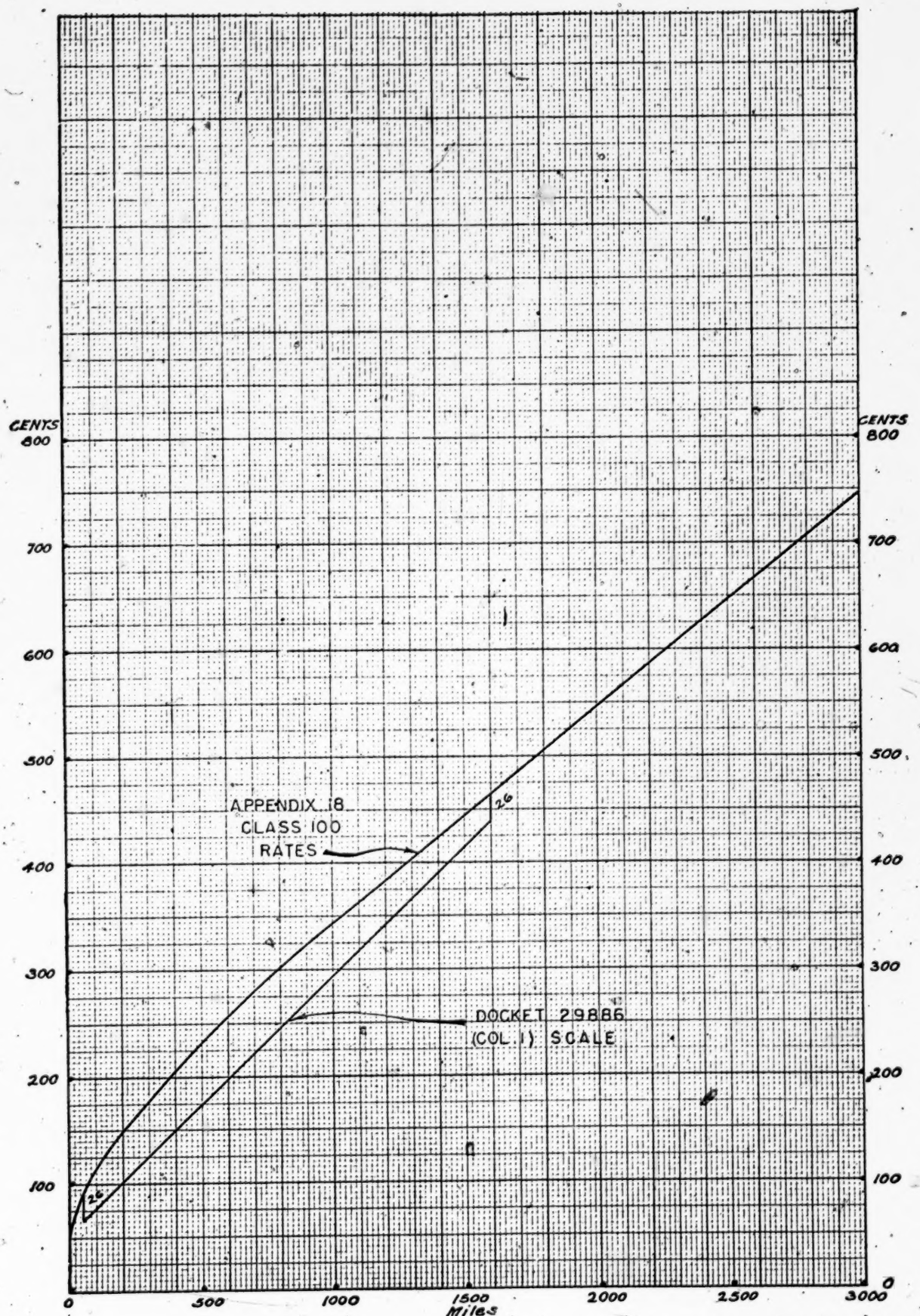
At the respective hauls of 500 and 600 miles, which approximate the average of the hauls involved in the Docket 29886, *Official-Southwestern,* and the Docket 28277, *Official Western Trunk Line* proceedings considered together, the differences in percentage divisions produced by the different scales are relatively small. The cost scale and the Docket 28277 scale differ by one percentage point, or $1 out of every $100 of revenue, with the Docket 29886 scale falling in between.

However, when these same scales are applied to the widely disparate long hauls characteristic of the transcontinental traffic, the differences in the results produced by the different scales become extreme, as shown by the following table based on the relative hauls of 600 and 2000 miles, the approximate average hauls of the Eastern and Western lines on transcontinental traffic:

	Docket 29886 Scale	Docket 28277 Scale	U. S. Average Cost Scale
Carrier A (600 miles)	27.0%	30.2%	24.7%
Carrier B (2000 miles)	73.0%	69.8%	75.3%

Thus, at the average hauls here involved, the differences between the cost scale and the Docket 28277 scale proposed by the Eastern and Midwestern lines amount to 5½ percentage points, or $5.50 out of every $100 of revenue, with the Docket 29886 scale also producing a substantial difference.

In order to explain the marked differences in revenue results produced by the application of the various integer scales to the transcontinental traffic, it is necessary to examine the basis upon which these scales are constructed, particularly in their relation to the longer hauls.



Source: Exhibit T-299, opp. p. 4

[fol. 803]

2. The Construction of the Docket 28277 and Docket 29886 Divisional Integer Scales from Class Rate Scales.

As stated in the report in *Official Western Trunk Line Divisions,* 269 I. C. C. 765, 777, the Docket 28277 divisional integer scale is based on the Appendix 10 class rate scale prescribed in the Docket 28300 *Class Rate Investigation,* 262 I. C. C. 447, 766. The Docket 28277 divisional integer scale differs from the Appendix 10 class rate scale only to the extent that a constant factor of 18 integers has been deducted from each mileage on the rate scale to produce the divisional integer scale. The factor of 18 integers represents one terminal handling (half of what the rate would be at zero mileage on the rate scale, which covers two terminal handlings).*

The Docket 29886 divisional integer scale is also derived from a class rate scale—the Appendix 18 class rate scale prescribed at a later stage of the Docket 28300 *Class Rate Investigation,* 281 I. C. C. 213, 328. The graph on the opposite page (now p. 649) shows the mechanics of the construction of the Docket 29886 scale: 26 integers represent the deduction of one terminal handling (half of what the rate would be at zero mileage on the Appendix 18 rate scale).** The 26 integers are subtracted from the Appendix 18 class rate scale at 50 and 1600 miles (the shortest and longest hauls covered by the Docket 29886 integer scale). The straight line drawn between these two points was used as the divisional integer scale in Docket 29886.

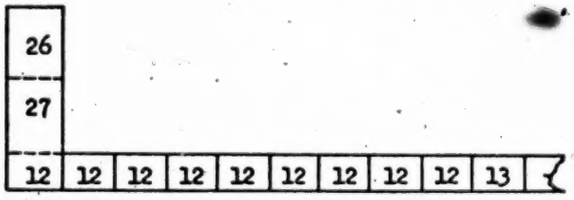
With its construction tied directly to the Appendix 18 rate scale, the progression of the Docket 29886 divisional scale necessarily reflects the progression of the rate scale. The Commission stated that the pattern of this particular integer scale "corresponds generally with that of" the Appendix 18 rate scale. *Official-Southern Divisions,* 289 I. C. C. 4, 7.

* At 20 miles the Appendix 10 class rate is 48 cents, at 15 miles 46 cents, at 10 miles 43 cents, and at 5 miles 40 cents, indicating by the retrogression that at zero miles the rate would be 37 or 36 cents, one half of which is about 18 cents (Exhibit T-302, Appx. B).

** At 10 miles the Appendix 18 class rate is 64 cents, and at 5 miles 58 cents, indicating by the retrogression that at zero miles the rate would be 52 cents, one half of which is 26 cents (Exhibit T-299, p. 5; Exhibit T-302, Appx. B).

RATES OF PROGRESSION IN NO. 29886 INTEGER SCALES

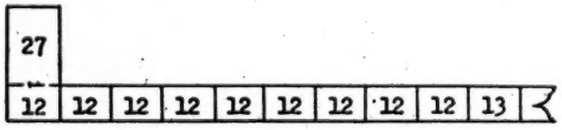
Column 1
(287 ICC 595)



Miles	0	50	100	150	200	250	300	350	400	450	500
Integers		65	77	89	101	113	125	137	149	161	174

Miles	Integer	Progression
50	65	
100	77	12
150	89	12
200	101	12
250	113	12
300	125	12
350	137	12
400	149	12
450	161	12
500	174	13
...	...	..
...	...	..
1750	475	12
1800	487	12

Column 2



Miles	0	50	100	150	200	250	300	350	400	450	500
Integers		39	51	63	75	87	99	111	123	135	148

Miles	Integer	Progression
50	39	
100	51	12
150	63	12
200	75	12
250	87	12
300	99	12
350	111	12
400	123	12
450	135	12
500	148	12
...	...	..
...	...	..
1750	449	12
1800	461	12

[fol. 804]

Source: Exhibit T-299, opp. p. 6

[fol. 805] The chart on the opposite page (now p. 651) shows the resulting elements of the Docket 29886 scale. The uniform progression of 12 integers per 50 miles, produced by drawing a straight line between the point 26 below the Appendix 18 class rate at 50 miles and the point 26 below the rate at 1600 miles, is shown as a series of blocks.* The terminal factor of 26 is shown in the initial block of the scale. An additional increment of 27 integers appears in the initial block of the scale.

The Docket 29886 scale for an intermediate, or bridge, haul (287 I. C. C. at 595, column 2), differs from the basic Docket 29886 scale only in the deduction of a second 26 integers (representing the remaining terminal handling).**

The residual 27 integer factor in the Docket 29886 scales has no logical basis; it is simply the mechanical result of starting with a first class rate of 91 cents at the 50 mile point of the Appendix 18 scale, deducting 26 as a terminal factor to produce 65 as the initial integer, and drawing a line to the 1600 mile point on the rate scale to produce a rate of progression of 12 integers per 50 mile block.

Witness Gilbert J. Parr's analysis of the elements of the Docket 29886 divisional integer scale in relation to cost of service shows that the 27 integer factor cannot be explained as representing way train costs, or interchange costs or any other element bearing upon the service performed (Exhibit T-299, pp. 6-10). 27 is simply the balance remaining in the initial mileage block, over and above the 12 integers representing 50 miles of line haul and the 26 integers representing one terminal handling. The 27 integers in the Docket 29886 scale thus represent the in-

---

* The method used in constructing the scale produced a rate of progression of 12.06 integers per 50 mile block. This accounts for the occasional rounding to 13 integers per 50 mile block at several points in the Docket 29886 scale.

** No intermediate scale was prescribed in Docket 28277, but the Midwestern lines have proposed an intermediate scale, calculated by deducting a second 18 integer terminal factor from the basic Docket 28277 scale (Exhibit MW-140, p. 1).

fluence of the rate scale progression in the Appendix 18 class rate scale from which the integer scale was derived.

These technical problems of scale construction were of relatively little significance in the Official Southwestern case in which the Docket 29886 scale was prescribed because the respective hauls then before the Commission were relatively short and nearly equal. However, this 27 integer factor, over and above the terminal factor, would [fol. 806] have an important effect on the percentage division if this scale were applied to long hauls which differ greatly in length. This is because the constant 27 integers are added for each application of the scale, however short or long the mileage, and this produces a higher allowance per mile for the short haul carriers (over and above that justified for terminal service) than for the long haul carriers.

3. The Historical Origin and Basis of the Use of Rate Scales in Constructing Divisional Integers Does Not Support, But Instead Refutes, the Effort to Apply Such a Scale to Very Long Haul Traffic Where the Commercial Taper in the Rate Scale Comes Into Play.

Divisional scales constructed from rate scales have been prescribed by the Commission in cases where the average hauls of the respective groups of roads have been relatively short.* In those cases, the Commission emphasized that a mileage prorate, which was the only systematic basis of divisions previously employed in making divisions, was unsatisfactory because it failed to take into account the relatively greater burden of terminal expense experienced by the short haul road. In the report on further hearing in the *New England Divisions Case,* 126 I. C. C. 579, 667, Commissioner Eastman stated that "it is because of this fact [the relative burden of terminal cost] that a rate

* See Exhibit T-299, Appendix B, for a comparison of relatively short hauls in the Docket 29885, 29886 and 28277 proceedings with the long and disparate hauls on transcontinental traffic.

prorate * * * affords a valuable test of divisions." This followed the Commissioner's earlier statement in *U. S. War Dept.* v. *A. & S. Ry. Co.*, 92 I. C. C. 528, 538-39:

> "* * * a dominant consideration must be the relative amount and cost of the service performed by the various participating carriers. * * *
>
> "The rate prorate basis is often an approximate means of dividing rates in accordance with the amount and cost of the service rendered, * * *"

Consistent with this use of the rate scale as measuring the relative amount and cost of service, both line haul and terminal, Commissioner Eastman based the construction of intraterritorial class rate scales on the best evidence then available showing the progression of costs, *Southern Class Rate Investigation,* 100 I. C. C. 513, 642-644, 647 (although the cost evidence then available was admittedly [fol. 807] incomplete, 109 I. C. C. at 305). See also *Consolidated Southwestern Cases,* 123 I. C. C. 203, 384-385.

Where the class rate scales prescribed for application to the relatively short intraterritorial hauls within the South and Southwest conformed to the progression of railroad costs on the basis of the evidence then available, it was logical, and preferable to the alternative of a mileage prorate, to use divisional integer scales based on such rate scales in prescribing divisions on traffic *where the average hauls of each contesting group were also relatively short.*

However, where longer hauls are involved, a different consideration, entirely foreign to the cost progression, controls the construction of the rate scale. This is the taper, or depressed rate of progression, which is characteristic of the longer reaches of rate scales and which is introduced to move traffic over the long hauls. This reduction below the progression of costs is dictated by commercial considerations inherent in moving long haul traffic. These traffic considerations, given effect by the

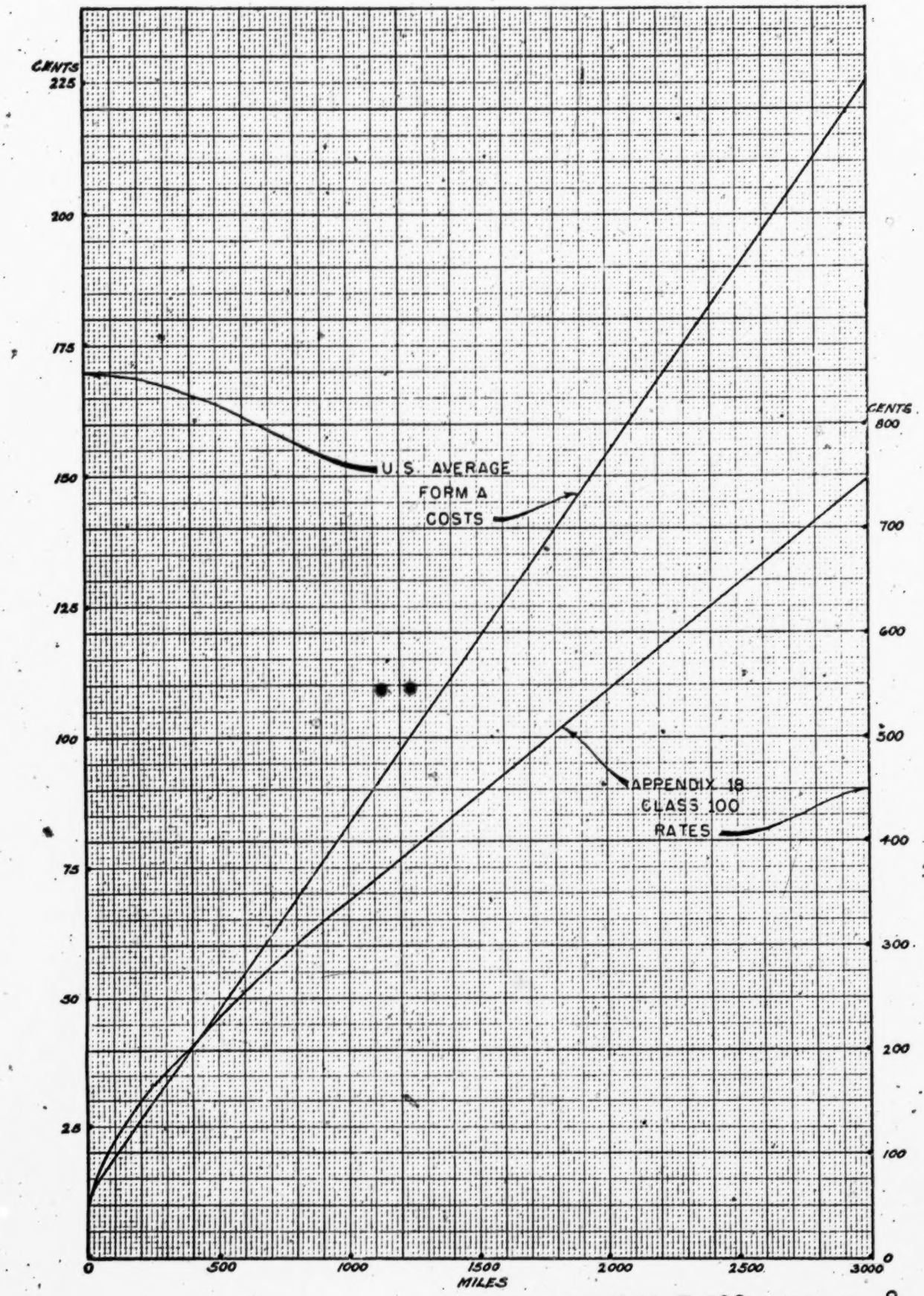
Commission and by the carriers in the construction of rate scales, are described on this record by Witness A. J. Stilling (Exhibit T-302, pp. 11-19).

The Supreme Court has recognized the Commission's practice of giving effect to traffic competitive considerations as distinguished from the cost of the haul at the longer distances, stating in *Ayrshire Collieries Corp.* v. *United States,* 335 U. S. 573, 590-591:

> "These differentials in the present case were not designed so as to be faithful to the factor of distance. The Commission followed the common practice in giving diminishing weight to distance and increasing weight to competition as the length of the haul increased."

As previously stated, the Appendix 10 and Appendix 18 class rate scales, respectively, are based, were prescribed in the Docket 28300 *Class Rate Investigation.* In that investigation, the Commission's staff presented a study of the construction of class rate scales; the Commission's report concluded its discussion of that study as follows (262 I. C. C. 447, 642):

> "A comparative study and analysis of the construction of various class-rate scales prescribed by us shows that usually they were of a pattern in which the greatest rate of progression was in the first 75



Source: Exhibit T-302, opp. p. 8

> [fol. 809] miles. The purpose was to reflect the relatively expensive service furnished by way-freight trains. Beyond 75 miles the progression was at a more moderate rate to reflect the relatively lower cost of through freight service. *In the longer reaches of the scales there was a still lower rate of progression for the purpose of permitting traffic to move long distances.* (Emphasis supplied.)

The graph on the opposite page (now p. 657) compares the progression of the Appendix 18 class rate scale with that of the Rail Form A United States Average cost scale. The graph shows that the progressions of the cost scale and of the rate scale are not substantially different for the first 600 or 700 miles. Beyond that, however, the rate scale reflects the taper or depressed rate of progression necessary to the movement of traffic over long distances. This depressed rate of progression of the Appendix 18 rate scale results in a steadily mounting difference between the rate scale and the cost scale which becomes extreme at the long hauls typical of the transcontinental movement.* The Commission made it plain that the difference between the progressions of the rate scale and of the cost scale did not reflect any doubt upon the accuracy of the constant progression of the Rail Form A cost scales introduced by the Commission's staff in Docket 28300 *Class Rate Investigation,* since the report emphasized: "Costs alone do not * * * control the contours of rate scales," 262 I. C. C. 447, 693.

The Rail Form A cost scale separates the rail costs into terminal and line-haul elements and provides for the further separation of the line-haul into way-train and through-train unit costs. Prior to the development of Rail Form A by its own Cost Finding Section, the Commission had considered cost scales based on a single uniform progres-

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* The degree of depression at the longer hauls here involved is somewhat more pronounced in the slope of the straight line of the Appendix 18 class rate scale than the tapering progression of the Appendix 10 scale (Exhibit T-302, p. 16 and Appendix E).

sion of all line-haul costs and, in 1939, had commented in *Southwestern-Official Divisions*, 234 I. C. C. 135, 138:

> "This assumption [that line-haul unit costs do not vary with distance] is commonly made by statisticians who undertake to make studies of average transportation costs in the form of distance scales. Whether the assumption is true is a question which remains to be answered."

[fol. 810] No such statement that the straight line progression of line-haul costs is an unproven statistical assumption can be made today. With a separation of way-train costs, the straight line progression of through-train costs reflected in the Rail Form A cost scales has been fully established in numerous studies made and reviewed by the Commission's Cost Finding Section since it was founded in 1939. These studies have been fully documented for this record and the nature of through train-line line-haul costs analyzed by Witness Gilbert J. Parr (Exhibit T-301). No evidence has been presented even questioning the straight line progression of through-train costs; the cost scales introduced by Witnesses Heywood and Carpenter for the Eastern and Midwestern lines, respectively, are themselves based on a straight line progression of cost (*e.g.*, Exhibit E-37; Exhibit MW-151).

In the cases in which the Commission has prescribed divisional integer scales based on rate scales, this method was deemed to be, in the words of Commissioner Eastman quoted above, "an approximate means of dividing rates in accordance with the amount and cost of the service rendered." For the relatively short intraterritorial hauls involved in such cases, the progression of the rate scale did approximate that of the cost scale and so achieved the intended result. But at the longer hauls, where the rate scale is depressed by traffic and not cost considerations, the very premise underlying the use of the rate

scale progression as an approximation of the cost progression condemns the use of a rate scale in making divisions.

Another argument that has been relied upon as supporting the use of divisional integers based on rate scales is that: "In shaping the progression of the divisional scale it is proper to take into account the distance progression of the rates to be divided. *Divisions of Freight Rates,* 156 I. C. C. 94, 98," *Official-Southern Divisions,* 289 I. C. C. 4, 6-7. For the reasons set forth herein, this theory is applicable only at the relatively short and approximately equal hauls where the rate scale progression approximates the cost progression, since the theory would produce confiscatory results if applied to the long and disparate hauls typical of the transcontinental traffic where the commercial depression of the rate scale comes into play. In any event, the concept of dividing the rates in a manner reflecting the distance progression of the rates to be divided has no application in this transcontinental divisions case. The transcontinental rates, including even [fol. 811] the transcontinental class rates, are not constructed in relation to a distance scale (Exhibit T-294, p. 13). Unlike the rates on Official-Southwestern traffic, for example, which moved on, or in fixed relationship to, a class rate scale, the transcontinental rates are governed by market and other competitive forces without relation to any distance scale (Exhibit T-294, p. 14). Indeed, the great volume of the transcontinental rates being divided in this proceeding do not progress upward with distance, but are blanketed for a thousand miles or more (Exhibit T-296, pp. 17, 40-45). Under such circumstances, the theory that the progression of rate scales may be used in making divisions because that is the way the rates being divided are made has no place in this transcontinental divisions case.

4. The Unfair and Confiscatory Effects of Using Rate Scales as the Basis for Divisional Integers on Long Haul Transcontinental Traffic.

As shown, the depressed or declining progression in the longer hauls of class rate scales does not reflect the progression of costs but is a deliberate departure from costs based on commercial and traffic considerations. This depression or taper in the rate scale is based upon the experience of the Commission and the carriers in arriving at the depression in long haul rates necessary to move traffic.

The depression in the long haul rate is made for the common benefit of all of the participating carriers. It is an inducement necessary to attract the business in the interest of the joint enterprise. Where the difference in the hauls of the participating carriers is extreme, as in the case of transcontinental traffic, it would be grossly unfair to determine the division of the long haul carrier by use of a rate scale reflecting the depression in long haul rates required to move the traffic. Such action would impose upon the long haul carrier the entire burden of the depression in the rate solely designed to attract the traffic producing the revenues to be divided. Since the tapering or depression below the cost progression is for the benefit of *all* lines participating in the through movement, and has nothing whatever to do with the *relative* contribution of those lines to the aggregate cost of handling the traffic, the depression or taper should be borne fairly and ratably by all of the lines and must not be imposed on the long haul carriers alone (Exhibit T-299, pp. 11-13; Exhibit T-302, pp. 17-18).

[fol. 812] The unfairness to the long haul carriers of making divisions by use of scales reflecting the rate scale taper was stressed by the Eastern lines at various stages of the Docket 28277, *Official Western Trunk Lines* proceedings where the Eastern lines had a somewhat longer haul than the WTL lines. The Eastern lines stated:

"Manifestly, rate progression as the basis for divisions would be ruinous to any group of railroads. * * * the lower value per mile reflected to the [long haul rate] is attributable to the combined through services of both groups of railroad—not to a part of the service to one group."

* * * * * * *

"Since the proportionate contribution of the two groups of carriers to the performance of the transportation should furnish the primary consideration in the determination of a reasonable divisional basis, and since that contribution of effort or expense can ordinarily be best measured by relative costs of service, it is of major importance that there be taken into account the progressions which relative costs of service would produce in a scale of divisional factors predicated thereon."

(Exceptions to Examiner's first report, pp. 77, 95, in Docket 28277, quoted in Exhibit T-299, p. 21, Appx. C, p. 1.)

"But here we have a predominance of long haul in the east and we say that your factors ought in some fashion to represent the relative amount of service as that can be reflected on a dollar basis. Moreover we think there is an inherent confusion of unlike things in saying that because rates may follow one progression that relative cost factors should do likewise, or that divisional factors should do likewise. There are many things that enter into the making of rates."

(Oral Argument of Counsel for Eastern lines, in Docket 28277 Tr. 533-535, quoted in Exhibit T-299, Appx. C, p. 3.)

These statements of the Eastern lines in the Docket 28277 proceeding, which accurately emphasize the unfairness of imposing the extra burden of the rate scale taper on the

long haul lines, are directly in point in this transcontinental divisions case involving widely disparate hauls on very long haul traffic.*

[fol. 813] The impropriety and the illegality of divisional integers based on rate scales as applied to transcontinental traffic is demonstrated by the effect of such scales in severely and inequitably reducing the rate of return of the long haul carriers relative to the earnings of the shorter haul participants in the traffic.

The effect on rate of return follows from the fact that the only margin in costs is the return factor. The operating expenses, rents and taxes incurred in handling any given carload of freight remain the same whatever the revenue. Thus, the effect of imposing the burden of the commercial depression in the rate scale progression upon the divisions of the long haul carrier is to transfer that carrier's fair share of the earnings to its short haul connections.

The effect of the different types of divisional integer scales upon rates of return was measured by Witness Gilbert J. Parr (Exhibit T-299, pp. 13-19). The following examples show the effect on the rates of return of the carriers where the respective hauls are 600 miles and 2000 miles (these being approximately the Eastern and Western hauls on transcontinental traffic). United States average Rail Form A costs are used for purpose of illustration in order to exclude the effect of differences in territorial

* The principles stressed by the East did not come into play to any such extent on the hauls in the Docket 28277, *Official-WTL*, proceeding itself. This is because the differences in hauls were relatively less important (676 miles East vs. 425 miles WTL, 269 I. C. C. at 779), and also because the average haul of the longer haul Eastern lines was only 676 miles, which is not far from the point in the class rate scale where the tapering of the scale for traffic reasons begins. Substantial differences between the rate scale and the cost scale do not develop until the greater distances found not in Official-WTL traffic, but on the transcontinental traffic here at issue.

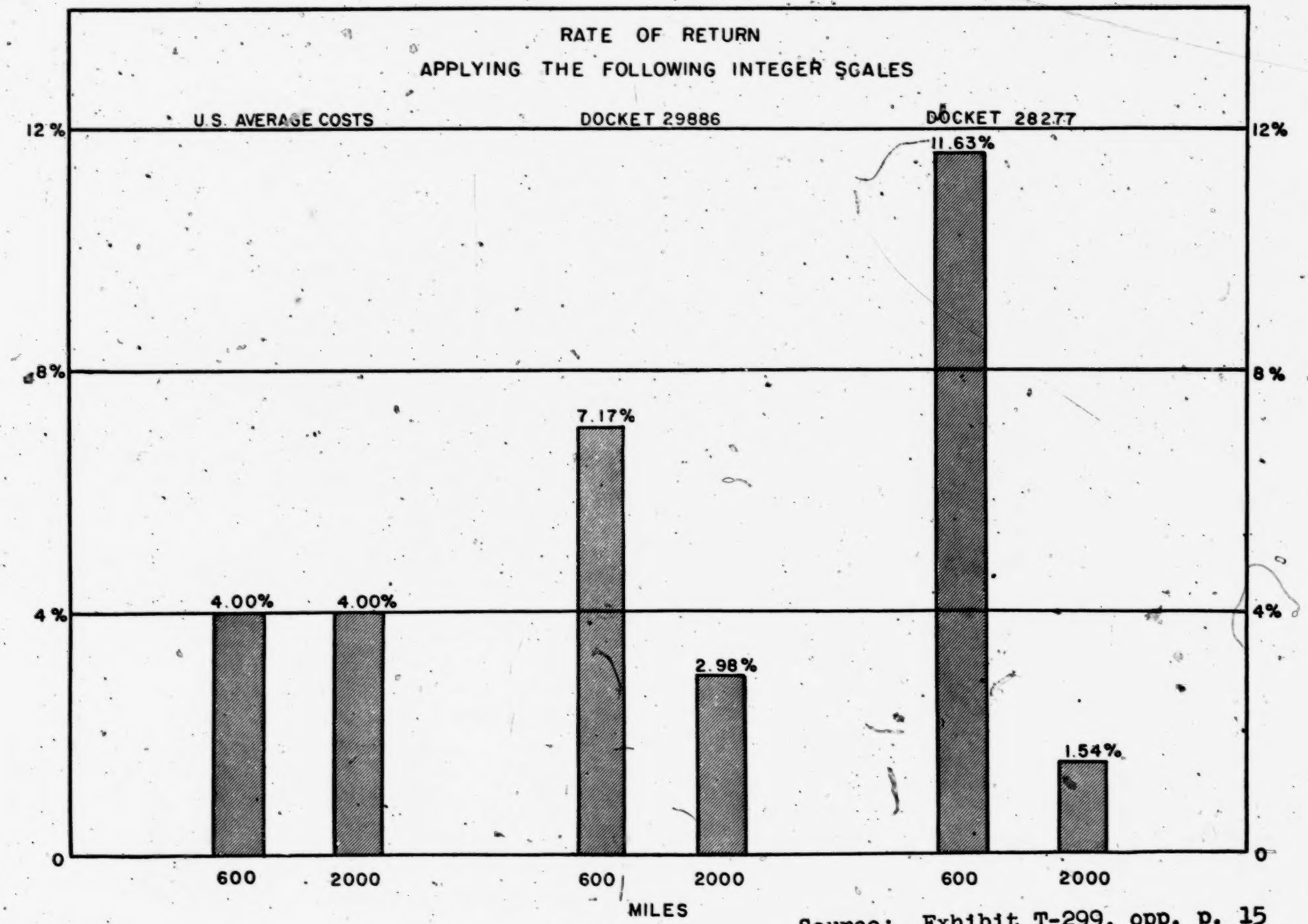
costs and revenue needs, and thereby to isolate and measure the effect of the different integer scales.

The following table shows the cost relationship at these hauls for an average car producing revenues assumed to be equal to the U. S. average fully distributed costs, including return (Exhibit T-299, p. 14):

Miles	Costs			Divisions (Per Cent)
	Operating Expenses Rents and Taxes	Return at 4%	Total	
600	$209.94	$ 27.55	$237.49	24.7%
2000	637.49	85.49	722.98	75.3
2600	$847.43	$113.04	$960.47	100.0%

In other words, $960.47 of through revenue, divided on the basis of the relative costs (24.7% and 75.3%) produces a uniform 4% rate of return for both the long haul and the short haul carrier participating in the haul of an average carload of freight.

[fol. 814]



Source: Exhibit T-299, opp. p. 15

[fol. 815] If, however, the Docket 29886 integer scale, reflecting the depressed progression of a rate scale at the longer hauls, is used to divide the same $960.47 of through revenue, the percentage distribution of the revenue would be $27.0% and 73.0% for the 600 and 2000 mile hauls, respectively. The operating expenses, rents and taxes (other than federal income tax) remain the same, with the following effect on rates of return (Exhibit T-299, p. 14):

Miles	Docket 29886 Divisions	Revenue	Costs Operating Expenses, Rents, Taxes	Return	Return Rate of
600	27.0%	$259.33	$209.94	$ 49.39	7.17%
2000	73.0	701.14	637.49	63.65	2.98
2600	100.0%	$960.47	$847.43	$113.04	4.00%

The result of applying the Docket 29886 integer scale is that the 600 mile carrier receives full reimbursement of its costs, including a return of 7.17%, while the return of the long haul carrier is reduced to only 2.98% (Exhibit T-299, p. 15), a plainly unlawful division of the 4% return included in the revenue for the entire through movement. The very construction of the Docket 29886 scale is such that, for substantially different lengths of haul, the return, which is the incentive of the service, is almost doubled for the short haul carrier and is reduced by more than one-fourth for the long haul carrier. The return of the short haul carrier becomes excessive, that of the long haul carrier confiscatory.

The chart on the opposite page (now p. 665) compares the rates of return produced by the cost scale, and the Docket 29886 scale, on hauls of 600 and 2000 miles, which are representative of the Eastern and combined Western hauls into

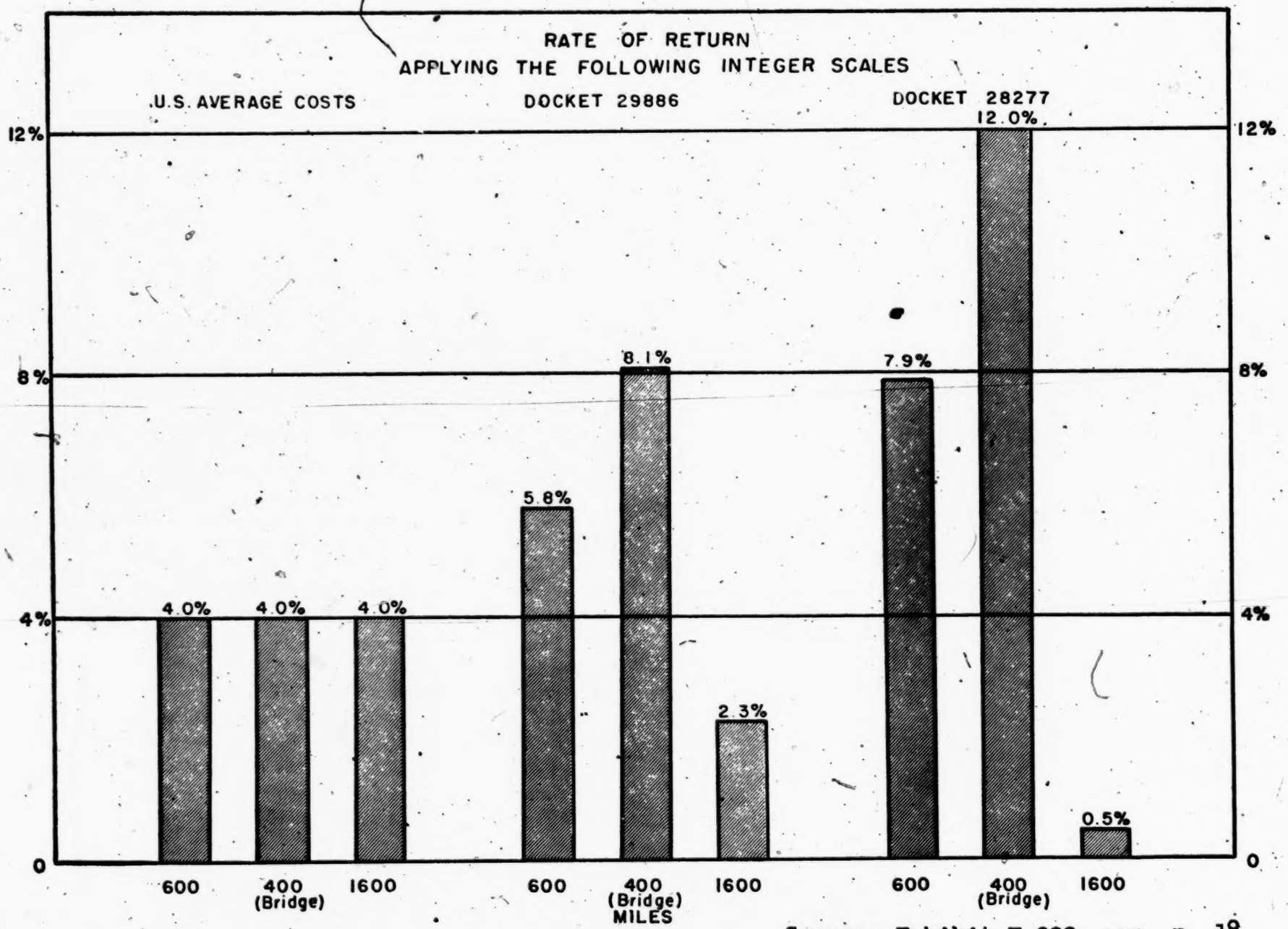
which the Eastern lines would break the transcontinental traffic.* The even more extreme distortion of rates of return resulting from application of the earlier Docket 28277 scale to the transcontinental hauls is also shown on this chart.

The depressing effect of the divisional integer scales constructed from rate scales on the rate of return of long

(Continued on page 670)

* The severe effect of the rate scale progression on rates of return of the long haul carriers would also result from application of these divisional integer scales to hauls of 500 and 1600 miles, the approximate average hauls of the Midwestern lines and the combined Midwestern and Mountain-Pacific haul of the Transcontinental lines on traffic originating and terminating in the Midwest (Exhibit T-299, p. 16).

[fol. 816]



Source: Exhibit T-299, opp. p. 18

[fol. 817] haul carriers is even more extreme where three groups of roads are concerned, as is the case on the most important volume of transcontinental traffic. The following examples are based upon hauls of 600 miles for the carrier performing origination and destination service in the East, 400 miles for an intermediate or bridge carrier in the Midwest, 1600 miles for the combined haul in Midwestern and Mountain-Pacific territory of the transcontinental lines performing originating and destination service in Mountain-Pacific territory. These examples again assume, for purpose of analyzing the effect of divisional integer scale construction, that the revenues are equal to United States average costs. On this basis, the cost relationships would be as follows (Exhibit T-299, p. 17):

	Cost Basis		Costs		
Miles	Divisions	Revenue	Operating Expenses, Rents, Taxes	Return	Rate of Return
600	24.7%	$237.49	$209.94	$ 27.55	4.0%
400	14.5	138.71	122.16	16.55	4.0
1600	60.8	584.27	515.33	68.94	4.0
2600	100.0%	$960.47	$847.43	$113.04	4.0%

In other words, division of $960.47 of through revenue on the basis of the relative costs (24.7%, 14.5% and 60.8%) produces a uniform rate of return for each of the railroads participating in the haul.

Application of the Docket 29886 integer scale, which reflects the rate scale rate of progression, would increase the division of the short haul terminal line and also increase the division of the bridge line, with the following effect on rates of return (Exhibit T-299, p. 17):

Miles	29886 Divisions	Revenue	Costs Operating Expenses, Rents, Taxes	Return	Rate of Return
600	26.0%	$249.72	$209.94	$ 39.78	5.8%
400	16.2	155.60	122.16	33.44	8.1
1600	57.8	555.15	515.33	39.82	2.3
2600	100.0%	$960.47	$847.43	$113.04	4.0%

As shown, division of the through revenue by use of the Docket 29886 integers reduces the rate of return for the long haul carrier to 2.3%; the rate of return of the short haul terminal line and of the bridge carrier are raised to 5.8% and 8.1%, respectively, in contrast to the 4.0% rate of return produced by the joint rate.

The chart on the opposite page compares the rates of return which would be produced by the assumed equal cost [fol. 818] scale, the Docket 29886 scale, and the earlier Docket 28277 scale where three groups of roads participate in the transcontinental haul. As shown, the integer scales based on the rate scale progression are markedly preferential to the short haul carriers, and particularly to the short haul bridge carriers. The chart also explains the particular interest of the Midwestern lines in proposing the earlier and more extreme Docket 28277 scale.

As between two carriers operating under exactly the same conditions and with identical costs, the integer scales prescribed in Dockets 29886 and 28277 would produce for the long haul carrier a rate of return from the joint service only a small fraction of that received by the short haul carrier. This result is inherent in divisional scales based on rate scales as applied to the very long hauls characteristic of transcontinental traffic. The taper or depression in the rate scale, made necessary solely by traffic and com-

mercial considerations affecting the entire through movement, has nothing to do with the relative services performed by the roads participating in the haul. When a rate scale is used to construct scales of divisional integers, such as the Docket 29886 and 28277 scales, it is inherent in the method that the entire burden of the depression in the rate which attracted the traffic is imposed on the long haul carrier. This produces the confiscatory results shown in the foregoing chart, with one participating carrier receiving from three and one-half to twenty-four times the rate of return of another for reasons which do not bear any relation whatever to their respective contributions to the joint service.

It is thus demonstrated that where the relative hauls are substantially different, the use of such integer scales would make a mockery of the legislative standard spelled out in Section 15(6). The very mechanics or method of stating the divisions completely dominates their measure rather than the mandate of the law.

* * * * * * *

[fol. 819] The Midwestern lines' proposal would also have the Commission prescribe divisions at interchanges between Mountain-Pacific roads at Ogden and Salt Lake City, Utah, 500 miles inside the Mountain-Pacific border. There is no justification for determining in this proceeding internal divisions within the Mountain-Pacific group of lines (Exhibit T-303, p. 13). Apart from the Commission's lack of jurisdiction over such divisions under the pleadings, the Midwestern lines' only legitimate interest in these proceedings is to obtain fair divisions for their own lines in their own territory, not to concern themselves over divisions within another territory.

* * * * * * *

[fol. 820]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

TRANSCONTINENTAL DIVISIONS CASES

No. 31503 and Sub. Nos.

THE AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY et al.

vs.

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, et al.

APPENDIX TO BRIEF OF MOUNTAIN-PACIFIC LINES AND REQUESTED FINDINGS—Filed June 13, 1960

S. R. Brittingham, Jr., R. Granville Curry, Frank S. Farrell, Lawrence W. Hobbs, Thormund A. Miller, Ernest Porter, Howard V. Rhedin, L. E. Torinus, Jr., E. L. Van Dellen, Howard J. Trienens, Douglas F. Smith, Counsel for the Mountain-Pacific Railroads.

Due Date: June 13, 1960.

[fol. 821] Requested Findings

* * * * * * *

[fol. 822] II. Efficiency.

1. To the extent that costs and earnings data reflect inefficient operations, the Act requires that such overstatement of efficient cost and understatement of true earnings capacity be given effective consideration.

2. To treat costs and earnings data which reflect inefficiency as if they were the result of normal opera-

tions, and to use such data as the basis for fixing future divisions, would reward inefficiency contrary to the purpose and express provisions of the Act.

3. The costs and earnings of the New York Central in recent years, and particularly for its 1956 operations, are acknowledged to have reflected wasteful duplication of yards and shops, obsolete yards, tracks and maintenance of way methods, and the effects of the topheavy and uncoordinated organization inherited from prior managements.

4. The costs and earnings of the Chicago and North Western, and particularly for its 1956 operations, are acknowledged to have reflected wasteful and inefficient maintenance practices, inefficient use of existing diesel power, duplicate facilities and other faulty techniques and procedures inherited from the prior management.

5. The present managements of the Central and C&NW have undertaken vigorous programs for the rehabilitation of their properties, but the programs which [fol. 823] will reduce costs and improve earnings have of necessity inflated operating expenses for recent years.

6. The cost and earnings data of record for the Central and C&NW do not reflect the true cost and earnings potential of those properties for use in comparisons with other carriers.

7. The costs and earnings of the Central and C&NW are improving relative to the Official and Midwestern group averages, respectively.

8. Cost comparisons between railroad groups based on the data of record should take account of the overstatement of costs of the Central and C&NW, now in the process of correction, and financial compari-

sons should exclude the temporarily depressed earnings of those two roads.

III. Revenue Needs.

A. General.

1. In the determination of divisions pursuant to the Act, the relative revenue needs of the respective groups of roads from the traffic at issue must be given consideration in the interest of the preservation and development of rail transportation to serve the public interest.

2. The Mountain-Pacific roads are dependent for half of their total system freight revenues upon revenues from the divisions of transcontinental traffic; the Eastern and Midwestern lines look to transcontinental traffic for only 6% and 17%, respectively, of their system freight revenues.

3. Mountain-Pacific territory has been and will continue to be the fastest growing territory in the nation, measured by changes in population and in terms of economic growth.

4. The Mountain-Pacific lines have experienced a substantial increase in the physical volume of traffic handled.

5. The traffic accounting for the increase experienced by the Mountain-Pacific roads has been transcontinental traffic moving on depressed rates.

[fol. 824] 6. Accompanying the increase in physical volume of traffic handled and the increase in gross revenues experienced by the Mountain-Pacific lines has been an even greater increase in expenses and in net investment which have combined to produce declining rates of return.

7. During the post-war period, the Mountain-Pacific lines have added over $1½ billion to their investment in railroad property without experiencing any additional earnings to support the added investment.

8. Taking account of all funds available and all funds required from railroad operations, the Mountain-Pacific roads produced only $61 million annually in funds available for their stockholders, providing a return of but 1.36% on the stockholders' investment in railroad property.

9. The imminent expiration of tax deferrals will reduce by two-thirds the margin of funds produced for stockholders by the Mountain-Pacific roads' railroad operations.

10. The need of the Mountain-Pacific roads for investment funds is continuing and increasing with the continuing rapid growth of the Mountain-Pacific territory.

11. A way must be found to increase the earnings of the Mountain-Pacific roads in order that their ability to meet the investment demands of the territory served not be impaired.

12. The increase in investment of the Mountain-Pacific roads has been at a far greater rate than the increase in investment of the Midwestern and Eastern roads.

13. The Midwestern and Eastern roads, serving relatively stable territories, are not growing but are stable or shrinking plants, important portions of which are being reduced to eliminate unnecessary facilities.

14. The Midwestern and Eastern roads are producing funds available as a return on their properties at a substantially higher rate than the returns experienced by the Mountain-Pacific roads.

15. Railroads in all territories rely on railroad earnings as a primary source of funds for investment in railroad plants.

[fol. 825] 16. The Mountain-Pacific lines have been increasing their debt while roads in other territories, principally Eastern roads, have been substantially reducing debt.

17. It would represent an unwise reversal of regulatory policy to base any decision on the premise that the Mountain-Pacific lines should not rely upon retained earnings for investment needs but should further add to their debt.

18. With the Mountain-Pacific lines under the necessity of devoting substantial funds to increased investment that produces no added return, additions to investment becomes a part of the real cost of serving the growing Mountain-Pacific territory.

19. Because of the sparsely settled terrain in the interior of Mountain-Pacific territory and the concentration of population and production at the Pacific Coast fringe of the territory, the traffic and rate structures on traffic to, from and within Mountain-Pacific territory are peculiar to that traffic.

20. The transcontinental traffic upon which the Mountain-Pacific lines are primarily dependent for their revenues is unlike any of the other freight hauls in the United States, because of its very long hauls and its distinctly different problems encountered in meeting most intense market and water competition.

21. The rates on the most important commodities moving transcontinentally have been subjected to repeated imposition of holddown treatment in general increase cases, and this has reduced the percentage increases realized on the very long transcontinental

traffic far below the increases realized by short and medium haul traffic.

22. The Mountain-Pacific roads are dependent for half of their system revenues on their divisions of transcontinental rates and, in turn, half of the transcontinental rates are subject to the depressing effect of holddowns, with the result that the prescription of holddowns prevents the Mountain-Pacific roads, to a far greater degree than the Midwestern and Eastern roads, from recovering their increased costs through increased rates.

[fol. 826] 23. Decentralization of industry, truck competition and other competitive factors of increasing intensity are reducing the revenue-producing quality of the transcontinental traffic.

24. The traffic moving within Mountain-Pacific territory produces 10 to 16% less revenue per ton and ton-mile than the non-transcontinental traffic available to the Eastern and Midwestern roads, respectively.

25. Much of the traffic moving within Mountain-Pacific territory consists of raw materials moving at low rates to produce transcontinental movement of processed commodities.

26. The balance of the traffic moving within Mountain-Pacific territory moves at rates depressed by the concentration of population and production along the Pacific Coast and by truck competition whose potential is greater than in other territories because of materially higher load and length limits.

27. Carriers in all territories have been confronted by increasing competition restricting increases in revenues during this period of inflationary cost increases, but the Midwestern and Eastern roads' traffic has produced increased revenues at a rate 25% greater than the increases produced by the trans-

continental and intra-Mountain-Pacific traffic, the only traffic available to meet the revenue needs of the Mountain-Pacific roads.

28. Because of the long hauls and competitive relationships affecting in exceptional degree the traffic upon which the Mountain-Pacific lines depend, the revenue position of the Mountain-Pacific roads will worsen with each round of cost increases, particularly in relation to the position of the Midwestern and Eastern roads.

29. The data of record bearing upon the revenue needs of the respective territorial groups of roads show that the return presently available to the Mountain-Pacific roads is at a substantially lower rate than for the Midwestern and Eastern roads, that Mountain-Pacific territory will continue to be the fastest growing territory requiring investment in railroad plant at a greater rate than the rest of the country, and that retained earnings will continue to be the principal source of investment funds.

30. In view of the public interest in maintaining and developing railroad transportation in the rapidly growing Mountain-Pacific territory and the primary [fol. 827] dependence of the roads serving that territory upon the transcontinental divisions for their revenues, the transcontinental divisions of the Mountain-Pacific roads should be increased.

B. Computation of Rates of Return.

1. The rates of return to which consideration should be given are those experienced in recent periods when comparatively normal conditions prevailed.

2. The rates of return of the Class I Mountain-Pacific roads are lower than the rates of return of the Class I Eastern and Midwestern roads.

3. Class II and Electric roads do not handle any appreciable volume of transcontinental traffic in the East or Midwest, but do originate or terminate 8% of the transcontinental traffic in Mountain-Pacific territory.

4. The rates of return of Class II and Electric roads handling transcontinental traffic are substantially lower than the rates of return of the Class I carriers in Mountain-Pacific territories.

5. The base regularly employed by the railroads in computing rate of return relates Net Railway Operating Income to the Net Investment in Transportation Property as shown in the accounts prescribed by the Commission.

6. Temporary tax deferrals, produced by rapid amortization of defense projects, results in the substantial but temporary inflation of net railway operating income for the year 1952 and subsequent years shown of record.

7. The extent of overstatement of net railway operating income due to temporary tax deferrals has been greater in the case of the Mountain-Pacific roads than for the Midwestern or Eastern roads.

8. Tax deferrals reached their peak during the years 1955 through 1958, and will virtually disappear by the end of 1960.

9. Elimination of the effect of tax deferrals from the earnings data for the years 1955 and 1956 is essential [fol. 828] in making practical and realistic estimates of the earnings relationships which will apply in future normal years.

10. Income and expenses attributable to non-railroad operations should be excluded as not pertinent to the issues in this proceeding.

11. The net railway operating income of the Pennsylvania and New York Central is understated for purposes of comparison with other roads by approximately $7 million annually due to the different accounting for equipment acquired through insurance company equipment leases.

12. The financial witnesses for each of the respective groups of roads have agreed that the adjustments in net railway operating income for tax deferrals, tax on nonrailroad income and insurance company equipment leases should be made in comparing the earnings of railroad groups.

13. The property base used in this proceeding is the net original cost to the carriers.

14. The base used by the Midwestern lines, and by the Eastern lines at a later stage of the hearings, referred to herein as the "Elements of Value" base, was copied from statements of the Valuation Section by adding figures labeled "Original cost (except land and rights)", "Present Value of land and rights", and "Working Capital including Material and Supplies", and deducting depreciation reserves appearing in the accounts of the carriers.

15. "Present value of land" as shown in the Valuation Section statements does not measure the original cost of land; nor is there any evidence supporting it as a measure of the present value of land.

16. There is no support in this record for the calculated figures for "Working Capital including Material and Supplies" as shown in the Valuation Section statements.

17. The "Elements of Value" figures do not cover the same property and are in other respects not maintained on a basis consistent with the depreciation accounts, and the revenue and expense accounts,

[fol. 829] prescribed by the Commission; the investment accounts are maintained on a basis consistent with the other accounts.

18. In the accounts prescribed by the Commission, the cost of property to the carrier is recorded in accounts entitled "Investment in Transportation Property".

19. Except for the pioneer Mountain-Pacific roads there is no substantial difference between road and equipment property as recorded in the investment accounts and as shown in the "Elements of Value" figures.

20. The figures shown in the Valuation Section statements under the heading "Original cost (except land and rights)" represent original cost for road and equipment property which was not in existence on valuation date and the cost of reproduction at the 1914 price level for property which was in existence on valuation date.

21. The theoretical reproduction of a railroad, such as is assumed in valuation work, is materially different from the original construction when the conditions at the time of original construction differed greatly from the conditions assumed at the time of theoretical reproduction.

22. At the time the theoretical reproduction cost data were being developed in the valuation work, the Commission expressly declined to develop an estimate of the cost incurred at the time the property was constructed.

23. At the time of their original construction in the East and Midwest, the railroads generally were built through settled areas following existing roads and canals and with adjacent sources of supplies and labor.

24. At the time of their original construction, the pioneer Mountain-Pacific lines were built through a mountain wilderness with no access to roads and canals and with supplies and labor requiring transportation over great distances.

25. Reproduction cost at the 1914 price level produces the substantial equivalent of the original cost of construction for the average road in the East and Midwest but, because of the very much greater dis- [fol. 830] parity between the conditions at the time of actual construction and the conditions assumed at the time of theoretical reproduction, reproduction cost at the 1914 price level substantially understates the cost of construction of the pioneer Mountain-Pacific roads.

26. Prior to this divisions case, all the roads, including the Eastern and Midwestern roads, had stated to this Commission that the reproduction cost figures at the 1914 price level did not measure the cost of construction for individual railroads and that the difference was highly accentuated for the pioneer Mountain-Pacific roads; all the roads also stated to the Commission that the reliability of the costs recorded in the investment accounts for early years may not properly be questioned by generalization but any such questions may be raised in any territory as to individual roads subject to the review and supervision of the Commission and its Bureau of Accounts under Section 20 of the Act.

27. The "Investment in Transportation Property" recorded in the accounts of the carriers maintained under the regulation and supervision of the Commission provides the measure of the railway property held for and used in the service of transportation which should be used as the property base, subject to the deduction of the depreciation reserve and the acquisition adjustment accounts.

28. Consideration of the acquisition adjustment account for reorganized roads is necessary to reflect the investment in road and equipment property of the carriers party to this proceeding.

29. To the extent that investment of the predecessors to reorganized carriers was eliminated in reorganization by the Commission and the Courts, nothing that the Commission can now do in this divisions case can provide a return to the former owners of that investment.

30. The relevant groupings of railroad figures for use in this transcontinental divisions case should not exclude roads participating in the transcontinental traffic, or give disproportionate weight to roads with [fol. 831] relatively little participation in the transcontinental traffic, but should reflect the degree of participation in the transcontinental traffic by each of the roads in each of the territories.

IV. Changes Since Divisions Were Established.

1. The transcontinental divisions of the Midwestern lines were the subject of the investigation instituted by the Commission in 1923 as Docket 15234.

2. The present transcontinental divisions of the Midwestern lines are the product of a settlement which increased the divisions of the Midwestern roads in 1925 following the initial hearings in Docket 15234.

3. The present transcontinental divisions of the Midwestern lines were the subject of further hearings in Docket 15234 on a 1929 record and were found not unreasonable or otherwise unlawful in the Commission's 1934 report in that proceeding.

4. In a subsequent reopening of Docket 15234 in 1939, the principal Midwestern lines declined to join in any complaint against the present divisions.

5. Since each of the base years significant in the establishment of the present transcontinental divisions of the Midwestern roads, the physical volume of traffic, the gross revenues, expenses and net investment of the Mountain-Pacific lines have increased to a greater extent than for the Midwestern lines, and the Net Railway Operating Income and the rate of return of the Midwestern lines has either increased to a greater extent, or decreased to a lesser extent, than for the Mountain-Pacific roads.

6. Since each of the base years significant in the establishment of the present transcontinental divisions of the Midwestern roads, the earnings position of the Midwestern lines has improved relative to the earnings position of the Mountain-Pacific lines.

7. The cost evidence before the Commission in Docket 15234 did not measure in any satisfactory way the relative costs of handling transcontinental traffic; such evidence bearing on costs as is available for that period indicates that the costs incurred by the [fol. 832] Mountain-Pacific lines in handling transcontinental traffic have increased relative to those of the Midwestern lines.

8. The present transcontinental divisions of the Eastern lines have never been prescribed or approved by the Commission.

9. The present transcontinental divisions of the Eastern lines are based upon an agreement, signed in April 1922, that increased the Eastern lines divisions as the price for their concurrence in reduced transcontinental rates which were essential to the transcontinental lines but a matter of indifference to the East.

10. The agreement of 1922 increasing the divisions of the Eastern lines to their present level was not the

product of an appraisal of relative costs, relative revenue needs or other lawful criteria, but was the result of the superior bargaining power of the Eastern lines.

11. Because the justice and equity of negotiated divisions are roughly proportionate to the degree of equality of bargaining power, the divisions embraced in the 1922 agreement were preferential to the Eastern lines.

12. Since the present transcontinental divisions of the Eastern lines became effective, the physical volume of traffic, the gross revenues, expenses and net investment of the Mountain-Pacific lines has increased to a greater extent than for the Eastern lines and the Net Railway Operating Income and the rate of return of the Eastern lines has increased to a greater extent than for the Mountain-Pacific lines.

13. Since the present transcontinental divisions of the Eastern lines became effective, the earnings position of the Eastern lines has improved relative to the earnings position of the Mountain-Pacific lines.

14. In the absence of a base period in which the present transcontinental divisions of the Eastern road were found reasonable or were otherwise presumably in proper adjustment, it is appropriate to consider changes since 1947-1949, the commonly accepted post-war base period.

15. Since 1947-1949, the physical volume of traffic, the [fol. 833] gross revenues, expenses and the net investment of the Mountain-Pacific lines have increased to a greater extent than for the Eastern lines, but the Net Railway Operating Income and the rate of return of the Eastern lines has increased while the rate of return of the Mountain-Pacific lines has declined.

16. No evidence is available measuring the relative costs of handling transcontinental traffic at the time the present divisions of the Eastern lines became effective or for any time prior to 1953; between 1953 and 1956, the relative costs of the Eastern lines declined relative to the costs incurred by the Mountain-Pacific lines in handling transcontinental traffic.

V. Relative Class Rate Levels.

1. The transcontinental class rates prescribed by the Commission are approximately 30% higher per mile for hauls within Mountain-Pacific territory than for the hauls in the Docket 28300 area east of the Rocky Mountains.

2. The higher level of class rates prescribed for transcontinental traffic after the prescription of the Docket 28300 basis, confirms and continues the Commission's practice of prescribing and approving reasonable maximum rates that are substantially higher per mile in Mountain-Pacific than for other territories.

3. The existing higher level of class rates prescribed by the Commission to, from and within Mountain-Pacific territory, as well as the existing divisions, are essential to even the present, inadequate return of the Mountain-Pacific lines.

4. The higher level of class rates in effect for hauls in Mountain-Pacific territory is consonant with the decisive evidence of record establishing the relative costs of, and the relative revenue needs from, the transcontinental traffic.

VI. Mechanics of Making Divisions.

1. The mechanics or form of the divisions to be prescribed should make effective a distribution of rev-

enue which is just and reasonable as measured by the substantive standards of Section 15(6); any mechanical or formal features of a divisional basis [fol. 834] which produce a different distribution of revenue are unlawful to the extent of such difference.

2. The present group basis of publishing transcontinental divisions is highly desirable in light of the competitive conditions affecting the routing of transcontinental traffic.

3. The provisions of the present Official-transcontinental divisions agreement requiring that local rates be observed as maxima, requiring that divisions be applied to assumed minimum rates, and setting forth other special divisional arrangements, should be eliminated.

4. The divisional integer scales prescribed in Docket 28277 and Docket 29886 reflect directly or correspond generally to the progression of class rate scales prescribed in Docket 28300.

5. The progression of the Docket 28300 class rate scales does not depart materially from the progression of rail costs at short or medium hauls (of less than approximately 750 miles) but the progression of the class rate scales becomes substantially lower than the progression of rail costs at the longer hauls.

6. Rail Form A provides a reliable separation of terminal and line-haul rail costs.

7. The straight-line progression of through train rail costs employed in Rail Form A has been verified and established in studies made by the Commission's Cost Finding Section.

8. The depressed progression of rate scales at the longer hauls is a feature not explained by terminal,

way train or interchange service or any other element bearing upon the relative contribution of the participating carriers to the joint service.

9. The depressed progression of rate scales at the longer hauls is for the purpose of permitting and encouraging traffic to move long distances and is therefore a merchandising factor in the sale of rail transportation.

10. The depression in long haul rates, being necessary to attract traffic, is in the interest of all carriers participating in the joint rates, and has no bearing on the relative service contribution by the participating carriers.

[fol. 835] 11. Use of divisional scales based on rate scales, if applied to the very long haul transcontinental traffic, would impose on the participating carrier with the longest haul the burden of the depression in the rate necessary to attract the traffic in the interest of all the participants.

12. Use of divisional integer scales reflecting the rate scale progression, applied to very long haul traffic, would depress the rate of return received by the longer haul carrier and inflate the rate of return earned by the carrier having the shorter haul, thus transferring to the short haul carrier the long haul carrier's fair share of the earnings from the joint haul.

13. The use of divisional scales reflecting the rate scale progression, if applied to very long haul traffic, produces an inherently confiscatory effect on the participating carriers with the longer haul.

14. The Mountain-Pacific lines have the longest haul on transcontinental traffic, depend for over half of their freight revenue on divisions from the very long haul

transcontinental traffic, and have no offsetting short hauls on other interterritorial traffic.

15. The use of divisional scales reflecting a rate scale progression would be confiscatory in its effect upon the Mountain-Pacific lines if applied to transcontinental traffic.

16. The Commission has never prescribed divisional integer scales based on rate scales in any divisions case in which the hauls were as long and widely disparate as they are in the transcontinental haul.

17. The transcontinental rates being divided in this proceeding are not constructed with reference to class rate scales or any other distance scales.

18. Differences in the points at which divisional integers are applied cause very great differences in the revenue distribution if divisional integers are based on rate scales, although such differences in revenues cannot be attributed to differences in services performed, revenue needs or any of the other criteria of fair divisions under Section 15(6).

19. Differences in the points at which divisional integers are applied do not materially change the distribution [fol. 836] of revenue if the divisional integers are based on the cost progression, and even those minor differences are eliminated if the costs are adjusted to reflect the circuity between the breaking points.

20. In this transcontinental divisions controversy between three territorial groups of roads, the divisions should produce a fair revenue distribution as between Mountain-Pacific, Midwestern and Official territorial groups of roads; on such minor portion of the traffic as moves on routes through the South, a fair division should be made for the Southern haul.

21. The prescription of integer scales by mileage blocks, in the interest of simplicity of application, should not affect the aggregate distribution of the revenues.

22. The average haul to and from each mileage block for each group of carriers approximates the midpoint of the block; use of the extreme end of the block in determining the value for the entire block consistently overstates the average haul.

23. Ascertainment of the integer for the mileage block by application of the integer scale to the extreme end of the 50-mile block gives each group of carriers credit, on the average, for 25 miles of service which it does not perform.

24. When hauls are long and widely disparate, as in the case of the transcontinental traffic, the addition of 25 miles to the haul of each group increases the percentage division of the shorter haul group without any justification in the relative services performed.

25. The purpose of a minimum percentage division was to protect the short haul carrier against the failure of a mileage prorate basis of divisions otherwise to compensate for terminal service.

26. Under a divisional basis properly constructed, and reflecting proper allowance for terminal, way train and other services performed, there should be no percentage minimum provision because any application of a minimum percentage would, by definition, defeat the application of a basis designed to produce fair divisions.

27. The mechanics or form of the divisions to be prescribed in this proceeding, reflecting the relative costs of the respective groups of roads in the handling [fol. 837] of transcontinental traffic, and reflecting the revenue needs of the respective groups of roads

as they depend upon the transcontinental traffic, should be such as to produce an increase of not less than 10% in the present transcontinental divisions of the Mountain-Pacific roads.

Conclusion.

1. Considering all the evidence of record, the present divisions of the joint rates on the traffic here involved are unjust, unreasonable, inequitable and unduly prejudicial as to Mountain-Pacific railroads and unduly preferential to the Midwestern and Eastern railroads.

2. An increase in the present divisions of the Mountain-Pacific railroads of not less than 10% is justified and required to produce just, reasonable and equitable divisions of the joint rates on the traffic here involved.

[fol. 838]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

NOTICE TO THE PARTIES

Exceptions, if any, must be filed with the Secretary, INTERSTATE COMMERCE COMMISSION, Washington, D. C., and served on all other parties in interest, within 90 days from the date of service shown above, or within such further period as may be authorized for the filing of such exceptions. At the expiration of said period for the filing of exceptions, the attached report and order will become the report and order of the Commission and will become effective unless exceptions are seasonably filed or the report and order are stayed or postponed by the Commission. To be seasonably filed exceptions must reach the Commission on or before the date they are due. If exceptions are filed, replies thereto may be filed within 45 days after the final date for filing exceptions. The stated specific time periods apply

to all parties and give full effect to Rule 1.21 (c) of the General Rules of Practice to the extent, if any, the provisions of such rules otherwise would be applicable to these proceedings. It should not be assumed that the recommended report and order have become effective as the report and order of the Commission until a notice to that effect, signed by the Secretary, has been served.

No. 31503[1]

AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY ET AL.

v.

ATCHISON, TOPEKA & SANTA FE RAILWAY COMPANY ET AL.

Decided .....

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1. Divisions of joint rail rates between eastern territory and mountain-Pacific territory found to be unjust, unreasonable, and inequitable. Lawful divisions prescribed.

2. Divisions of joint rail rates between midwestern territory and transcontinental territory, including subdivisions of joint rates between eastern territory and transcontinental territory for transportation in mid-

[1] This report embraces also No. 31503, (Sub No. 1), Ahnapee and Western Railway Company et al. v. Abilene & Southern Railway Company et al.; No. 31503, (Sub No. 2), Chicago, Burlington & Quincy Railroad Company et al. v. Abilene & Southern Railway Company et al.; No. 31503, (Sub No. 3), Chicago, Milwaukee, St. Paul and Pacific Railroad Company v. Abilene & Southern Railway Company et al.; No. 31503, (Sub No. 4), Louisville and Nashville Railroad Company v. Akron, Canton & Youngstown Railroad Company et al.; and No. 31503, (Sub No. 5) Cincinnati, New Orleans and Texas Pacific Railway Company v. same.

western territory, found to be unjust, unreasonable, and inequitable. Lawful divisions prescribed.

Joseph F. Eshelman, W. T. Pierson, M. C. Smith, Jr., A. C. Armstrong, R. G. Bleakney, Robert D. Brooks, J. Raymond Clark, J. T. Clark, Robert B. Claytor, R. E. Costello, Eugene S. Davis, K. A. Dobbins, A. P. Donadio, J. W. Grady, Allen Lesley, K. H. Lundmark, Robert H. Pratt, Richard H. Stokes, and *Frank F. Vesper* for complainants in No. 31503.

[fol. 839] *Bryce L. Hamilton, Nye F. Morehouse, Nuel D. Belnap, John W. Adams, Jr., Thomas M. Beckley, Martin L. Cassell, Charles H. Clay, Richard M. Freeman, George W. Holmes, John E. McCullough, Richard Musenbrock, William A. Thie,* and *Erle J. Zoll, Jr.* for complainants in No. 31503, (Sub No. 1).

J. A. Gillen for complainants in No. 31503, (Sub No. 2).

R. K. Merrill for complainant in No. 31503, (Sub No. 3).

E. R. Leigh for complainant in No. 31503, (Sub No. 4).

Arthur J. Dixon for complainant in No. 31503, (Sub No. 5).

Toll R. Ware for a cross-complainant in No. 31503.

Douglas F. Smith, Howard J. Trienens, S. R. Brittingham, Jr., R. Granville Curry, Frank S. Farrell, Lawrence W. Hobbs, Thormund A. Miller, Ernest Porter, Howard V. Rhedin, L. E. Torinus, Jr., and *E. L. Van Dellen* for transcontinental defendants.

W. C. Dowdy, Jr., and *Clyde W. Fiddes* for other defendants.

Thomas W. Dench, Joseph F. Nigro, A. O. Sheldon, James A. Robischon, J. G. Allard, Ingram B. Pickett, Lloyd Hammel, Hal S. Bennett, John J. O'Connell, Frank P. Hayes, William M. Bennett, Roderick B. Cassidy, J. Thomason Phelps, and *Cyril M. Saroyan* for interveners.

[fol. 840]

RECOMMENDED REPORT AND ORDER BY HOWARD HOSMER AND OREN G. BARBER HEARING EXAMINERS—Served December 6, 1960

These proceedings, consisting of a principal complaint and 5 others subnumbered, as well as certain cross-complaints, present the question of the lawfulness of divisions of joint rates for railroad transportation between points in mountain-Pacific territory and points in the rest of the conterminous United States except southern territory. There are 3 principal groups of litigants with mutually adverse interests, eastern railroads, midwestern railroads, and transcontinental railroads.

The eastern lines (sometimes hereinafter called the complainants) include most of the rail carriers of all classes assigned for statistical purposes to the eastern district and the Pocahontas region. The midwestern lines (complainants in one of the cases and defendants in others) are rail carriers which operate solely or mainly in that part of western territory which is east of the Rocky Mountains, the class-I railroads in this group being the following: Chicago and North Western Railway Company; Chicago Great Western Railway Company; Chicago, Rock Island and Pacific Railroad Company; Duluth, South Shore and Atlantic Railroad Company; Green Bay and Western Railroad Company; Gulf, Mobile and Ohio Railroad Company; Illinois Central Railroad Company; Kansas, Oklahoma & Gulf Railway Company; Lake Superior & Ishpeming Railroad Company; The Minneapolis & St. Louis Railway Company; Minneapolis, Northfield and Southern Railway; Minneapolis, St. Paul & Sault Ste. Marie Railroad Company; Missouri-Kansas-Texas Railroad Company and its Texas subsidiary; Missouri Pacific Railroad Company; and St. Louis-San Francisco Railway Company and its Texas subsidiary. The transcontinental lines (sometimes hereinafter referred to as the defendants) are railroads of all classes which operate wholly or partly west of the Rocky Mountains, including the following class-I carriers: The

Atchison, Topeka and Santa Fe Railway Company and its Texas subsidiaries; The Denver and Rio Grande Western Railroad Company; Great Northern Railway Company; Northern Pacific Railway Company; Southern Pacific Company and certain of its subsidiaries (not including the St. Louis Southwestern Railway Company); Spokane International Railroad Company; Spokane, Portland and Seattle Railway Company; Union Pacific Railroad Company; and The Western Pacific Railroad Company and its subsidiaries.[2]

The State regulatory commissions of 10 of the 11 mountain-Pacific States[3] were permitted to intervene in support of the defendants. One of these, the Wyoming Public Service Commission, later declared its neutrality. The Arizona Corporation Commission did not intervene.

Hearings extended intermittently from April 26, 1955, to December 11, 1959. Direct testimony was principally in writing contained in the exhibits, of which there were 834. Oral testimony, mainly on cross-examination, made up the transcript of 11,242 pages. Briefs filed by the 3 groups of principal rail carriers covered 1,145 pages plus voluminous appendices. The requests for findings in these briefs not discussed herein nor reflected in our recommendations and conclusions have been considered and found not justified.

[fol. 841] *No. 31503 and Sub-numbers 4 and 5*—The principal complaint was filed April 5, 1954, by the eastern lines, and the defendants therein are chiefly the western rail carriers whose lines connect directly or indirectly with those of the complainants. The divisions assailed in this complaint as unreasonable, inequitable, and unduly prejudicial and preferential under section 15(6) of the Interstate Commerce Act are those of joint rates between eastern territory and points in the 11 mountain-Pacific States subject to unimportant exceptions listed in note 4.

The transcontinental lines filed an answer to this complaint combined with a cross complaint in which they allege that the divisions assailed in the prineipal complaint are

[2] For this note and succeeding ones see Appendix A.

unjust, inequitable, and unduly prejudicial to themselves. Separate answers and cross-complaints similar to those of the transcontinental defendants were also filed by the Chicago, Burlington & Quincy Railroad Company (CB&Q) and its subsidiaries and also by the Chicago, Milwaukee, St. Paul and Pacific Railroad Company (CMStP&P).

The complaints in Sub Nos. 4 and 5 were filed by the Louisville and Nashville Railroad Company (L&N) and the Southern Railway Company (Sou) and a subsidiary, which operate in part between Ohio River cities and East St. Louis, Ill., and therefore have an interest in the divisions involved in the principal complaint. They attack those divisions on the same grounds relied on in that complaint.

The Missouri-Illinois Railroad Company (MI), assigned to the eastern district for statistical purposes, named as a defendant in No. 31503, with its answer filed a cross-complaint against all other defendants, which in practical effect makes it a co-complainant in that case. The transcontinental defendants responded to that cross-complaint with one of their own and also filed cross-complaints in Sub Nos. 4 and 5.

Sub Nos. 1, 2, and 3—The complaint in Sub No. 1 ranks with No. 31503 as one of the two major components of this litigation. It was filed by the midwestern lines June 3, 1954, naming as defendants the eastern and the transcontinental lines. Therein the midwestern lines assail as unreasonable, inequitable, and unduly prejudicial their divisions of (1) joint rates between eastern territory and that part of mountain-Pacific territory known as transcontinental territory as to which they perform intermediate service and (2) joint rates between transcontinental territory and midwestern territory.[5]

In Sub Nos. 2 and 3 the CB&Q and the CMStP&P, respectively, and certain of their subsidiaries allege that they participate in the joint rates and transportation involved in Sub No. 1 and ask that they be granted the same relief as may be accorded the complainants in that docket.

The transcontinental defendants are also cross-complainants in Sub No. 1.

Traffic Between Eastern and Mountain-Pacific Territories —For the purpose of estimating the amount of revenue produced by the rates subject to the divisions here in issue the parties made traffic studies based on actual movements in 1953 and 1955. The eastern lines undertook to measure all carload traffic between eastern and mountain-Pacific territories covered by interline settlements in October 1953. The defendants applied a sampling process to abstracts of waybills of carload shipments in 1953 and 1955. Certain other differences in the scope of these studies are of little [fol. 842] practical importance. As a whole, the studies indicate that, if 1953 and 1955 may be considered representative years, the traffic between these territories amounts to an annual volume of 910,000 carloads or 22.9 million tons, and yields about $890 million in annual revenue. These figures do not include less-carload traffic, which equals about 1.5 percent of the carload tonnage. Eastbound traffic predominates, accounting for 63 percent of the carloads, 70 percent of the tons, and 56 percent of the total revenue.

The primary commodity classifications of the carload traffic are represented by the following approximate percentages:

	Cars Percent	Tons Percent	Revenue Percent
Products of agriculture	26	19	19
Animals and Products thereof	1	1	1
Products of Mines	3	4	2
Products of Forests	22	29	20
Manufactures and Miscellaneous	44	45	55
Forwarders' Traffic	4	2	3
	100	100	100

Although the parties do not agree as to the proper method of estimating representative average hauls within the respective territories, it is a fair conclusion that the average movement in eastern territory is 600 miles and in western territory is 2,000 miles, based on short-line distances. From this it would appear that the complainants perform approximately 23 percent of the total service, measured by short-line ton-miles. The same percentage represents their share of the joint revenue as indicated by the defendants' traffic studies, the shares of the midwestern lines and the defendants being 15 percent and 62 percent respectively. The shares of individual carriers in the group totals as estimated by the defendants for 1953 are shown below.

Complainants			Midwestern Lines		
	Revenue (000)	Percent		Revenue (000)	Percent
NYC	$ 40,778	21.0	CRI &P ..	$ 21,601	17.2
Penn	39,703	20.5	CB&Q ..	19,446	15.5
Erie	18,047	9.3	C&NW	15,883	12.7
Wabash	17,884	9.2	Mo Pac ..	13,809	11.0
B&O	17,846	9.2	T&NO	10,327	8.2
NYC& StL ..	15,308	7.9	StL SW ..	9,506	7.6
C&O	9,248	4.8	IC	6,290	5.0
NYNH &H ..	3,699	1.9	T&P ..	5,426	4.3
LV	2,810	1.4	CGW ..	3,635	2.9
DL&W	2,253	1.2	StL SF ..	3,351	2.7
B&M	1,726	.9	M& StL ..	2,063	1.7
Rdg.	1,442	.7	GM&O	1,737	1.4
N&W ..	1,017	.5	MKT ..	1,717	1.4
C&EL ..	957	.5	GB&W	544	.4
Others	21,279	11.0	Others	9,984	8.0
Total	$193,997	100.0	Total	$125,319	100.0

	Defendants	
	Revenue (000)	Percent
AT&SF	$139,803	27.0
UP	130,200	25.0
SP	118,570	22.9
GN	37,036	7.1
NP	36,176	7.0
D&RGW	19,416	3.7
WP	12,774	2.5
CMStP&P	7,669	1.5
Others	17,196	3.3
Total	$518,840	100.0

[fol. 843] (The foregoing figures for the defendants reflect an understatement as the showing for the CMStP&P is incomplete.)

The great majority of cars included in the studies were interchanged between eastern and western lines at Chicago, Ill., St. Louis, Mo. (including East St. Louis, Ill.), and Peoria, Ill. The Chicago interchange was over 60 percent and as much as 64 percent including certain other junctions in the Chicago area. That at St. Louis was at least 18 percent and at Peoria 3 percent (increased to 7 percent with the addition of other interior Illinois cities). About 2.6 percent moved by car ferry across Lake Michigan. There was a negligible movement of about 0.3 percent or less through southern territory. A fairly substantial amount, 7 or 8 percent was interchanged by the Wabash at Kansas City, Mo., and other midwestern points.

It appears to be a sound estimate that about 27 percent of the traffic received a one-line haul west of the interchange points. Principally this would apply to the movements over the AT&SF and the CMStP&P, but it appears logical also here to take account of the CB&Q, a subsidiary of the GN and the NP, and the StLSW, and the T&NO, which are parts of the SP system.

The traffic in which the midwestern lines participate is interchanged between them and defendants largely at Council Bluffs, Iowa, (including Omaha, Nebr.), Kansas City, El Paso, Texas, the Twin Cities (Minnesota Transfer, Minneapolis, and St. Paul, Minn.), and Colorado Junctions (chiefly Denver and Pueblo). The defendants' study shows that average western hauls of this traffic in 1953 were 548 miles over midwestern lines and 1,666 miles over transcontinental lines. The study of the midwestern lines for that year shows an average haul of 702 miles for them and 1,603 miles for transcontinental lines.

The movements to and from the subdivisions of eastern territory were represented by the following percentages of total tons: central, 55.1; trunk line, 35.5; New England, 9.4. The revenue percentages were about the same. From the defendants' 1953 study it appears that about 36 percent of the cars originated or terminated in the metropolitan districts of the 4 major Pacific Ports, Seattle, Wash., Portland, Oreg., San Francisco and Los Angeles, Calif.

More than 90 percent of the movement between eastern and mountain-Pacific territories is in boxcars and refrigerator cars. The corresponding percentage for the more diversified traffic to and from midwestern territory is 82 percent. The percentages for the various types of equipment are shown in the following table:

Type of Car	Between Mountain-Pacific Territory and— Eastern Percent	Midwestern Percent
Box	61.27	60.75
Flat	2.38	3.10
Stock	.14	3.78
Gondala or hopper	4.96	7.47
Tank	1.35	3.60
Refrigerator	29.84	21.21
Special	.06	.09
	100.00	100.00

[fol. 844] *Traffic Between Transcontinental and Midwest Territories*—Because of differences in the scope of the traffic studies of the defendants and the midwestern lines it is impossible to estimate closely the volume of movement and revenue involved in Sub No. 1. The midwestern study indicates a movement of 330,000 cars between these territories in 1953 and a total revenue of $264.6 million. The broader study of the defendants includes the intermountain region not covered by this complaint and railroads which are not complainants therein. It shows a movement of 787,549 cars in 1953 and total revenue of $634.8 million. It appears from the two studies that the directional movements were about 60 percent eastbound and 40 percent westbound.

The midwestern study shows the following distribution of volume and revenue among the primary commodity classes:

	Cars Percent	Revenue Percent
Products of Agriculture	18.5	15.6
Animals and Products	6.9	5.0
Products of Mines	6.4	5.0
Products of Forests	30.3	28.7
Manufactures and Miscellaneous	34.5	43.3
Forwarder Traffic	3.4	2.4
	100.0	100.0

The most important points of interchange between the defendants and the midwestern lines are (in the order of importance) Kansas City, Council Bluffs, El Paso, Twin Cities and Colorado junctions. According to the midwestern lines' study the average haul per car for them was 695 miles and for the defendants, 1,568 miles. The revenue was divided 26.58 percent to the midwestern lines and 73.42 percent to the defendants. The average hauls shown in the defendants' study were 620 miles for the midwestern

lines and 1,488 miles for the defendants, and the respective shares of revenues were 25.9 percent for the former and 74.1 percent for the latter.

The revenue interests of individual carriers in the midwestern-mountain-Pacific traffic according to the defendants' study are shown below.

Defendants			Midwestern Lines		
	Revenue (000)	Percent		Revenue (000)	Percent
UP	$129,592	27.6	CB&Q	$ 37,083	23.1
SP	107,873	22.9	CRI &P	22,794	14.2
AT&SF	75,913	16.1	C&NW	16,185	10.1
GN	38,649	8.2	MP	16,019	10.0
NP	37,842	8.0	T&P	10,915	6.8
D&RGW	29,395	6.3	T&NO	7,799	4.9
CM&StP	16,592	3.5	StL SF	5,631	3.5
WP	15,759	3.4	IC	4,890	3.1
Others	18,714	4.0	MKT	4,375	2.7
			StL SW	3,448	2.2
	$470,329	100.0	CGW	2,087	1.3
			GM &O	1,627	1.0
			M&StL	1,073	0.7
			GB &W	105	0.1
			Others	26,254	16.3
				$160,285	100.0

For the purpose of these proceedings 3 subdivisions of midwestern territory have been designated as follows: Midwest east—Iowa, Wisconsin, the upper peninsula of Michigan, southeastern Minnesota, northwestern Illinois, and northern Missouri; Midwest southwest—Arkansas, [fol. 845] Louisiana, Oklahoma, Texas, southern Missouri,

and eastern New Mexico; and Midwest northwest—Kansas, Nebraska, South Dakota, southwestern Minnesota, and eastern Colorado. The percentages of total movement to and from these subdivisions were east 60 percent, southwest 33 percent, and northwest 7 percent.

The Present Divisions and Their History—The transcontinental joint-rate structure is the oldest in the United States. The joint rates between the Pacific coast and Midwestern Territory date from 1874, 7 years after the completion of the first transcontinental rail route. Those between official territory and the Pacific coast were established in 1887.

For most of that time the divisions of these rates have been a source of recurring controversy between the defendants, on the one hand, and the midwestern lines and the complainants, on the other. The earliest divisions were based upon some form of constructive mileage prorate in which the factors for distances west of the Missouri River were 150 percent of actual distances and those east thereof were actual distances. Because of their long hauls this basis was highly favorable to the defendants,[6] who also contended that their distance inflation was necessary to compensate them for adverse mountain grades and light density of population and traffic. These views have always been dominant in the thinking of the defendants and are reflected in their contentions here.

There were numerous changes of a minor nature in the divisions of the rates to and from official territory between 1887 and 1921. During much of that period the eastern lines' divisions of rates to and from New York City and other points on the Atlantic Seaboard were 25 percent (via Chicago), 27.5 percent (via Peoria), and 29 percent (via St. Louis). How these divisions were arrived at is not known. It may be only a coincidence that the Chicago division was equivalent to a constructive mileage prorate with a western inflation of 25 percent.

In 1922, the complainants and the defendants entered into a formal agreement concerning the divisions of the

eastern transcontinental rates as well as the measure of some of the rates. The eastern shares were increased but in such slight amounts, in our opinion, as not to support the contention of the defendants that they were forced to yield to the superior bargaining power of the complainants. The eastern divisions established by that agreement and now in effect are shown below:

Territorial Group	Divisions East of Chicago Percent	Peoria Percent	St. Louis Percent
New England-Seaboard	27.5	31	31.5
Truck-Line Interior (Syracuse, N. Y.)	25	28.5	29
Bessemer, Pa.	18	21.5	21.5
Buffalo-Pittsburgh	16.5	20	20
Cincinnati-Detroit (northern)	16	19.5	19.5
Cincinnati-Detroit (southern)	13	16.5	16.5

The above divisions are subject to certain maxima which need not be specified here. They apply generally on all traffic. There are certain special divisions on lumber to central territory generally higher than the general per- [fol. 846] centages. To the remainder of official territory special divisions apply only on rough lumber. On fresh fruit and vegetables to New England and New York City pier stations a deduction of about 6 cents per 100 pounds before prorating accrues to the eastern lines as a result of the Commission's decisions in *Erie R. Co.* v. *Alabama & V. Ry. Co.*, 98 I.C.C. 268. Thereby, for example, the complainants receive 29.3 percent of the rate on lettuce from the Pacific coast to New York City instead of the general percentage of 27.5 percent.

The percentages of the defendants from eastern-transcontinental rates to and from such places as Phoenix, Ariz., Spokane, Wash., and Reno, Nev., are the same as those of the rates to and from the Pacific ports. Apparently all of transcontinental traffic is thus blanketed. It may be inferred that the intermediate cities were considered commercially unimportant when joint rates were originally established. Consequently the revenue received by the defendants from shipments to or from the intermediate territory is relatively greater than the amounts which they receive on traffic to or from the port districts. Spokane, for example, is 295 miles east of Seattle, but the defendants' percentage of rates on Spokane traffic is the same as that on Seattle traffic. That percentage, applied to rates to and from New York City via Chicago and the Twin Cities is 60.2 for the service to and from the latter point. The difference of 295 miles before mentioned is 17 percent of the distance from the Twin Cities to Seattle and 7 percent of the distance from New York City to that point.

Since the preponderance of the midwest-transcontinental movement is to and from midwest-east territory, as before pointed out, the divisions received by the midwestern lines for their relatively short hauls between the Missouri River terminals and the Twin Cities, on the one hand, and Chicago, St. Louis, and other intermediate points, on the other hand, have long been a major bone of contention between the midwestern lines and the defendants. At the time when divisional controversies could only be settled by agreement the defendants were able to prevail on the midwestern lines to accept their time-honored constructive mileage prorate with the 50 percent inflation of the defendants' distances. Under this method the rates between transcontinental territory and Chicago were divided by apportioning 15 percent for the haul between the Missouri River or the Twin Cities and Chicago, and 11 percent between the Missouri River and St. Louis.

In 1923 the Commission on its own initiative instituted an investigation of the lawfulness of divisions of railroad

rates in the western district, commonly known as No. 15234, apparently in recognition of its relation of "fostering guardianship",[7] imposed by the 1920 legislation. There were hearings in that proceeding concerning the reasonableness of the transcontinental-midwest divisions but before submittal of the issues to the Commission for determination the two contending groups of carriers reached an agreement, effective July 1, 1925, under which the midwest divisions were generally increased 10 percent, yielding about $3 million additional revenue to the midwestern lines. This agreement had the effect, among other things, of raising the midwest Chicago division of 15 percent before mentioned to 16.5 percent and the St. Louis division of 11 percent to 12.1 percent.

[fol. 847] Following that action the investigation in No. 15234 was not discontinued, however, and in 1929 the Commission reopened it for further hearing concerning the transcontinental-midwest divisions. A decision on the further hearing was rendered in 1934, *Divisions of Freight Rates,* 203 I.C.C. 299, in which after stating some shortcomings in the evidence the Commission stated its conclusions at page 335, as follows:

> However, this case must be decided on the basis of the evidence of record, voluminous but most unsatisfactory; and there is no other way of deciding it than by the exercise of general judgment after consideration of this evidence, such as it is. Upon consideration of all the evidence of record, we are unable to find that the divisions of the transcontinental rates are unlawful.

Once again in 1940 the Commission reopened No. 15234 for the purpose of another look at the transcontinental-midwest divisions but after the start of the further hearings war conditions made further consideration of the question impracticable and No. 15234 was later discontinued "without prejudice."

In describing the divisions which resulted from the 1925 agreement the Commission in its 1934 decision said that "on the whole they happen to be slightly less than would result from a weighted-average mileage prorate in which actual distances east of the gateways are used in connection with a constructive distance of 1.25 miles for each mile west thereof." The defendants' 1953 traffic study indicates that similarly measured the average inflation west of the gateways would now be 19 percent. In some instances, however, the defendants' divisions are less than they would be under a straight mileage prorate. For example, the divisions of rates between Dallas, Tex. and Seattle via Kansas City are 30 percent south and 70 percent west of the interchange point, the respective distances being 473 miles and 1,906 miles. A mileage prorate would produce percentages of 20.3 south and 79.7 west.

Like the official-transcontinental divisions, the midwestern-transcontinental divisions are blanketed over all of transcontinental territory. Accordingly, for example, on a shipment from Chicago to Boise, Idaho, via Council Bluffs the UP receives the same division of 83.5 percent as it receives on a shipment to Seattle, 482 miles farther. This makes the Boise divisions equivalent to those which would result from a constructive mileage prorate using a constructive distance of 1.85 miles for each actual mile west of Council Bluffs.

The midwestern-transcontinental divisions of rates to and from Chicago, St. Louis, and other points of interchange with eastern lines are also used in subdividing the western shares of the official-transcontinental rates. Thus the western division of 72.5 percent of the rates between New York City and Pacific ports is subdivided by allowing the midwestern lines for the service between Council Bluffs and Chicago 12 percent (16.5 percent of 72.5 percent) and the defendants 60.5 percent (83.5 percent of 72.5 percent). When the movement is via St. Louis and Kansas City for the haul between those points the midwestern lines receive

8.3 percent (12.1 percent of 68.5 percent) and the defendants 60.2 percent (87.9 percent of 68.5 percent).

[fol. 848] The divisions of joint rates to and from Montana points via northern gateways in issue in Sub No. 1 do not conform to any uniform pattern and, in some instances, the general basis is in dispute. It is therefore not feasible to undertake any brief description of them here.

RELATIVE COST OF SERVICE

It is well-established that relative cost of service is a vital factor in the determination of just divisions, particularly those of interterritorial rates. Of course, it is a vital factor also in prescribing comprehensive rate structures, such as those of class rates, when comparative transportation conditions in two or more broad territories must be considered. To aid the solution of problems of this kind, the Commission's Cost Finding Section devised Rail Form A, which has been widely accepted as a sound and fairly understandable means of comparing relative transportation costs.

The major part of the huge record in the instant cases pertains to relative costs of service and raises an issue as to the extent to which Rail Form A computations reliably indicate such costs without extensive modifications and substitutions. In general, the complainants and the midwestern lines rely on Rail Form A, seeing no need for substantial departures therefrom, while the defendants urge that, although Rail Form A is a useful guide, there is an imperative need for extensive, special supplemental studies and substitutions to adapt it to the distinctive characteristics of transcontinental traffic.

The complainants applied Rail Form A to the accounts of the railroads in the eastern and western districts and used those applications to devise cost scales for the two districts in 50-mile blocks for different types of equipment with various loads shown in their traffic study for October 1953. Later, they submitted another scale based on defendants' traffic sample for 1956. The factors shown for the eastern

lines in this scale for distances up to 1,000 miles are on the average approximately 25 percent higher than those for the western carriers. The underlying costs are on the fully-distributed basis, including a 6-percent return on ICC elements of value and less depreciation and excluding passenger and less-carload deficits. If divisions were based on this scale, the complainants on an average would receive 29.5 percent of total revenue instead of 24 percent as settled. It is this showing upon which the complainants urge that divisions should be prescribed so as to afford them 32 percent of the total official-mountain-Pacific revenue, taking into account the rise in their costs since 1957.

The midwestern lines applied Rail Form A to the operating expenses and statistics of each group of railroads separately for the years 1953-1955 to develop group fully-distributed costs, including less-carload and passenger deficits, and return at 4 percent on elements of value after Federal income taxes. The groups were as follows: Eastern district, Pocahontas region, the principal Midwestern complainants, and the principal Transcontinental defendants. These unit costs, by years, were applied to traffic units of the same year taken from the Commission's waybill statistics. The traffic covered was to and from transcontinental territory only, and no cognizance was taken of statistics of carriers in midwestern territory other than those which are complainants in Sub No. 1. This study shows cost percentages for participants in official-transcontinental traffic as follows: [fol. 849] Eastern, 24.87; midwestern, 22.51; transcontinental, 52.62. The respective as-settled revenue percentages shown in the study were 21.63, 19.78, and 58.59. For midwestern-transcontinental traffic this study shows the following cost percentages: midwest, 32.58; transcontinental, 67.42. The respective as-settled revenue percentages were 26.77 and 73.23. The midwestern lines also devised two divisional scales, based on their cost computations, one for official-transcontinental traffic and the other for midwestern-transcontinental traffic. The first of these is a 3-way scale, in whic for distances up to 1,000 miles the eastern factors

average approximately 18 percent higher than the western factors. In their 2-way scale for midwestern-transcontinental traffic the two sets of factors are substantially equal.

The defendants' cost study is referred to in some detail *infra*. It was also used by them as a basis for cost scales. In their 3-way scale for official-mountain-Pacific traffic the factors in the first 10 hundred-mile blocks for the mountain-Pacific carriers on the average are 22 percent higher than those for the official lines. In the 2-way scale the mountain-Pacific factors are 43 percent higher than those for the midwestern carriers.

For purposes of comparison representative distances for the traffic to and from official territory are 600 miles in official territory, 700 miles in midwestern territory, and 1,600 miles for mountain-Pacific territory. There are shown below the percentages for those distances which would result from the scales before described.

	Eastern Percent	Western. Percent
Complainant's study	26.7	73.3

	Eastern Percent	Midwestern Percent	Mountain-Pacific Percent
Midwestern lines' study	25.5	23	51.5
Defendants' study	22.7	16.9	60.4

For a similar comparison relating to midwest-transcontinental divisions: representative distances are 700 miles for midwestern lines and 1,600 miles for those in mountain-Pacific territory. The percentages for such distances under the scales of those carriers are as follows:

	Midwestern Percent	Mountain-Pacific Percent
Midwestern Lines' study	32.4	67.6
Defendants' study	26.6	73.4

The traffic tests made by the defendants indicate that the revenue now received by carriers in the 3 territories from the divisions under consideration amounts to 47 percent of the total carload freight revenue of the defendants, 15 percent of that of the midwestern lines, and 6 percent of that of the complainants. The percentage relations to total ton-miles are approximately the same, except that in midwestern territory the ton-mile percentage is 19. The defendants consider these figures very important for several reasons. They find support therein for their assertion that any changes in the present divisions will have much more important consequences for them than for their opponents. They also urge that, since Rail Form A reflects conditions [fol. 850] affecting average movements it is essential to make allowance for the fact that transcontinental traffic accounts for a much larger proportion of defendants' total freight business than it does for the corresponding totals of the midwestern lines and the complainants.

The defendants concede upon the showing in their cost studies that the application of Rail Form A without adjustments produces costs for mountain-Pacific railroads which are substantially accurate, but argue from their studies that the actual costs in official territory are 19 percent below the Rail Form A unadjusted costs and that those in midwestern territory are 20 percent below.

For a proper application of the principles of Rail Form A, defendants undertook "the assembly in full detail of the operating service units which measure the amount and kind of service rendered on a representative sample of transcontinental movements, and the application to these service units of unit costs developed through Rail Form A, with substitution of direct costs wherever proper and feasible." The propriety and feasibility of those substitutions were the subject of a major part of the testimony and exhibits.

To assemble the operating service units the defendants obtained a subsample of the sample of individual carload movements which constituted their 1953 traffic study. The selection was by a scientific process and resulted in the des-

ignation of 7,380 carloads as representative, 3,226 carloads between official and mountain-Pacific territories and 4,154 between midwest and mountain-Pacific territories. Some of defendants' officials then endeavored to ascertain, as best they could, the probable routes traversed in detail by the sample cars in each of the territories in order to estimate the extent of branch-line movement, the comparative use of way and through trains, origin, destination, and interchange switching, as well as other services. Data for 7 of the sample cars were presented in an exhibit to illustrate the methods followed in computing costs for the entire sample. In the defendants' initial study operating expenses for 1953 were the basis of the computation. Later in the hearings the defendants presented another study, which is similar in a general way to the first but is marked by some important differences.

The end product of the defendants' first study was a purported showing that on cost proportions the revenue from the 7,380 carloads would have been divided as follows: Mountain-Pacific carriers, 63.25 percent; midwestern carriers, 22.67 percent; eastern carriers, 14.08 percent. The actual shares of the revenue as settled were 63.65 percent to the mountain-Pacific carriers, 22.99 percent to the midwestern carriers, and 13.36 percent to the eastern carriers. In the 1956 study, based on statistics for that year, the showing of revenue divided on cost proportions was as follows: Mountain-Pacific, 63.82 percent; midwestern, 21.61 percent; eastern, 14.57 percent. The shares as actually settled were: Mountain-Pacific, 63.76 percent; midwestern, 22.24 percent; eastern, 14.00 percent.

By way of rebuttal of the showing in the defendants' 1953 cost study the midwestern lines made a study of line-haul services which could be measured from actual records, including wheel reports, dispatchers' train sheets and time slips of their trains which contained the cars covered by the defendants' sample. They also made a study of the switching minutes in terminal service attributable to a random [fol. 851] subsample of that sample. The items of line-haul

cost embraced in the midwestern lines' special study represent about 25 percent of the total, of such items, and the elements of terminal service studied are about 50 percent of the total for such service. The study purports to show that if the terminal expense of the midwestern lines is adjusted to reflect the distinctive conditions disclosed by the study, the corresponding unadjusted figure would be increased 20 percent, and the adjustment in the line-haul expense, a much larger figure, would produce a reduction of 4 percent. The net result of the adjustment for terminal and line-haul expense combined is an increase of 0.1 percent, which is negligible. The midwestern lines therefore argue that, insofar as it is possible to make a direct assignment of costs to individual shipments, the unadjusted figures arrived at by application of Rail Form A must be accepted as accurately measuring the proportionate expense to the midwestern lines in their handling of intraterritorial traffic between points on their lines and those of the defendants.

The evidence relating to the cost studies of the defendants and the midwestern lines is the principal cause of the excessive size of the record, which unfortunately gives some support to the current criticism that administrative proceedings are becoming unwieldy, time-consuming, and expensive for all concerned. It is defendants' boast that their 1953 study "is undoubtedly the most detailed and comprehensive study ever made of the handling of a large body of railroad traffic," being the work of more than 730 people, who devoted to it more than 170,000 manhours of effort. In addition to the detailed testimony of the cost analysts who planned the studies and supervised their compilation evidence was presented by many other witnesses pertaining to operating, statistical, engineering, and mathematical aspects of the projects. By way of criticism of those studies the complainants and the midwestern lines also introduced voluminous evidence of the same general nature. Much of the testimony on this phase of the cases was essentially

argument of the cost analysts, including off-setting charges and countercharges of inconsistency on the part of these witnesses with positions taken in other proceedings. Much of it also had to do with correction of clerical and other errors.

The preparation of the studies entailed the accumulation of large quantities of working papers containing underlying figures and other data. The parties made available to one another all or a considerable part of these working papers for inspection or copying, and if that had not been done, the studies would have been largely unintelligible. In later stages of the hearings, copies of numerous working papers were reproduced as exhibits, but apparently the greater part of the working papers were not made a part of the record. Counsel were unwilling to agree to a stipulation that all such papers be considered as in evidence. The defendants' counsel thereupon sought to introduce a voluminous bundle of working papers not already in the record, but this evidence was excluded for reasons explained in Appendix C.

The defendants are no doubt correct in their assertion that no cost study comparable to theirs in scope and detail had ever before been presented in a proceeding before the Commission. They lay great stress on the fact that the study was modeled to some extent on studies made by our Cost Finding Section for special use in other proceedings of past years. One such was for a case involving a divisions complaint which was dismissed before final decision. The other was considered in *New Automobiles in Interstate Commerce*, 259 I.C.C. 475, in which the Commission's staff [fol. 852] submitted a study of rail costs of handling 175 typical shipments (contrasted with the 7,380 shipments studied by the defendants here.) An important circumstance is the fact that the studies above-referred to were organized and supervised by neutral public officials.[8]

It is manifestly impossible within the scope of this report to undertake a comprehensive critique of the cost studies or

even to restate briefly all of the points on which there is disagreement. Resolution of the controversial points, if at all possible, would be a lengthy and probably unrewarding job for a committee of neutral technical experts. Only a few of the principal questions and our impressions thereon will be mentioned.

The defendants assert that shipments between transcontinental territory and the other territories involved in these cases require proportionately more way-train service in transcontinental territory than in the other territories and that this circumstance necessitates a departure from Rail Form A, based on system averages which reflect a greater proportion of way-train service in the other territories.[9] The defendants' operating officials were able to ascertain the actual movement of the cars embraced in their traffic sample by way or through trains from their own records. The assignment of the cars to way or through trains of midwestern and eastern lines was based upon judgment of a committee of operating officials supplemented by time tables, maps, and other information of a public nature. Both the complainants and the midwestern lines presented evidence showing a considerable number of examples of erroneous assignment by the defendants' officials. We are therefore unable to accept the defendants' showing as conclusive on this point.

Furthermore we do not agree with the defendants that the complainants' use of Rail Form A territorial average costs applied to average-weight trains is necessarily unfair to the western lines. The table below sets forth certain figures for official territory relied on by the defendants and comparable figures for the western district.

Line No.		Official territory		Western District	
		Way trains	All trains	Way trains	All trains
	Car-miles—loaded cars (Statement No. 6-57):				
1.	Eastern district (thousands)	7,683	115,201		
2.	Pocahontas region (thousands)	1,885	28,328		
3.	Total (thousands)	9,568	143,529	13,793	186,281
4.	Percent of car-miles in way trains	6.67%	100.00%	7.40%	100.00%
5.	Average haul (miles)		630		2,259
6.	Car-miles in way trains imputed by use of average train costs (line 4 x line 5)	42		167	
7.	Traced car-miles in way trains in sample	9		34	
8.	Excess of imputed way train car-miles	33		133	
9.	Percentage of imputed to actual miles (line 6 ÷ line 7)	467%		491%	

[fol. 853] This tabulation supports the defendants' assertion that costs are somewhat overstated in official territory because average train costs reflect a greater proportion of the higher way-train expense than that assigned to the sample. However, the complainants' cost application was consistent for both territories, and the same effect in slightly greater degree is reflected in the western-district costs. The excess number of way-train miles is small compared to the average (33 against 630 and 133 against 2,259). The proportion is almost the same in each territory, and the effect on the cost relationship between the two territories would therefore be almost nil.

The cost relationship between the transcontinental and the midwestern lines might superficially appear to be affected by the use of average-train costs because the difference between the relative amounts of way train service in their territories is somewhat greater than the difference between the transcontinental and the eastern lines. However, even here the effect is minor because of the small amount of way-train service compared to the length of haul.

An important point of controversy between the defendants and their opponents is whether Rail Form A unadjusted maintenance-of-way and other roadway costs, averaged on a gross-ton-mile basis using a national average percent variable without reflecting differences in density, as used by the complainants and the midwestern lines is proper. It is contended that such costs understate the expense incurred for lines of light density and thereby cast upon that portion of the transcontinental traffic which traverses midwestern territory "in main line bridge service" the cost of maintaining light-density lines, is seldom, if ever, used for traffic of that kind. According to the defendants, "the Rail Form A unadjusted procedures assign to branch lines in the Midwest a total maintenance cost of only $197 per mile, of which $39 (20 percent) is treated as the constant expense per mile." The defendants consider this figure much too low, saying that "with the develop-

ment of a reliable figure representing the average constant cost per mile of track, the balance of the maintenance-of-way and return costs should properly be treated as variable costs for association with the movement of particular traffic. . . ." They further urge that "for application of costs based on 1956 operations, a fair and realistic figure to use as the constant cost of maintaining a line of railroad is $989 per track-mile." This figure is largely derived from returns to questionnaires filed with the Commission in abandonment proceedings. The problem presented is highly technical and complicated. An authoritative solution would apparently call for exhaustive engineering research. For that reason we are unwilling to accept the defendants' theories. We find no support therefor in *Lumber, California and Oregon to California and Arizona,* 308 I.C.C. 345, or any other decision of the Commission.

There was a considerable amount of evidence on the question whether the gross-ton-mile basis of allocating fuel cost and other items of locomotive expense used in Rail Form A is appropriate in estimating the cost of transporting transcontinental traffic. In their 1953 cost study the defendants followed a theory which has been advanced by the SP for many years, namely that fuel required by a diesel locomotive varies with grades and curves of track and that fuel consumption can be estimated by computing the energy (expressed in foot-pounds) required to traverse a given segment of railroad, using an average of 0.032 or 0.033 gallons of diesel fuel per million foot-pounds of energy output. The defendants originally took the position that the formula could also properly be used to relate [fol. 854] locomotive repairs to fuel consumption. Later they concluded that either gallons of fuel consumed or unit miles provided a reliable measure of locomotive repair costs, and they now request a finding that the energy formula is accurate for use in assigning locomotive fuel costs, whereas "the Rail Form a unadjusted costs substantially overstated the cost of fuel consumed by through trains carrying transcontinental traffic in the midwest and East."

The Commission has considered the energy formula in other decisions and has not been disposed to accept it with approval. Nothing in the present record, as we see it, would justify any change in that attitude.[16]

In Rail Form A, the allowance for return is at a rate of 4 percent after payment of Federal income taxes computed at current tax rates. The complainants and the midwestern lines urge that income taxes be disregarded, but on this question the defendants, being subject to relatively high income taxes, adhere to Rail Form A. That adherence, however, does not extend to acceptance of the 4-percent rate of return. The railroads as a whole, for sometime, have taken the position that the proper rate should be 6 percent. As the midwestern lines in the instant proceedings have used the 4-percent rate, they are criticized by the defendants for inconsistency. (The complaints apparently agree that the proper rate is 6 percent, since they have used it in their studies.) In our opinion, there are persuasive reasons for disregarding income taxes and using a 6-percent return, but the current thinking of the Commission seemingly supports the view reflected in Rail Form A. Further discussion of the question would not be justified.

A great deal of the record relates to the merits of certain gathering studies presented by the defendants, purporting to show the costs of originating rail shipments of lumber and perishables (fruit and vegetables) in mountain-Pacific territory. From the standpoint of hindsight, it may now be doubted whether the time and money spent by the defendants in preparing the studies and by the other parties in criticizing them were justified. Certainly the gathering studies were involved in an excessive amount of hearing time.

A total of 30 special gathering studies were made by the defendants, and apparently these were started in an early stage of their preparation before the parties had become impressed with the desirability of employing sampling procedures in such studies. Defendants say that they were satisfied that the studies "covered major gathering areas."

Later it turned out that a considerable number of representative shipments embraced in their cost studies had not originated in the previously selected gathering areas, but the defendants point out that, "cars from non-study areas were applied costs based on study areas with like operating obtain from their "traffic people" information concerning usual in such situations, there was much argument on this point, which involves the process technically called "imputation."

In the defendants' 1953 study, branch-line costs were computed on a fully-distributed basis, that is, at the level of 100 percent of operating expenses, rents and taxes, plus 100 percent of a 6-percent return on net book investment after income taxes. In their 1956 study, however, this basis was limited to traffic originating on their branch lines, "on which 50 percent or more of the cars originated and terminated are related to transcontinental traffic." The nature of this relationship was not disclosed in the defendants' testimony concerning that study, but the explanation came later in the rebuttal evidence of the other parties based on examination of the defendants' working papers.

[fol. 855] It was there shown that letters had been sent to attorneys for the principal defendants requesting them to conditions * * * on the basis of operating judgment." As the kind of traffic handled on the branches for the purpose described in the following excerpt from the letters:

> The intention is to treat costs on these branches as "solely related" to transcontinental traffic were 50 percent or more of the cars actually moved to or from transcontinental points, where the addition of cars reconsigned, diverted or transited will make the total 50 percent or greater and where the addition of cars of raw materials, one step back from the manufacturing process, to the cars actually moving transcontinentally or transited, etc., will boost the figure to 50 percent or better. Examples of raw materials that are related to outbound manufactured products are logs to lumber,

pulpwood to paper grain to grain products, sugar beets to sugar etc.

It appears that the boosters for the individual lines had difficulty in understanding the meaning of the expression "raw materials one step back from the manufacturing process." Some of them included coal, sand, fluxing stone, and fuel oil. In some instances the response was based on 1953 and in others on 1956. Also the people charged with the determination in some cases relied on interviews with shippers for their information as to the proportion of transcontinental traffic. We are unable to accept the theory that a proportion of 50 percent of such traffic on a branch indicates such a degree of dependence thereon as to justify the 100-percent assignment of costs, as the defendants contend. Nor were the methods employed in arriving at the percentage of transcontinental traffic such as to inspire confidence in the correctness of the purported result.

There is respectable authority for the view that fully-distributed costs and not out-of-pocket costs alone are of significance in divisions cases, but the contending parties here differ as to the method of utilization. The difficulty arises because of the fact that as yet the cost analysts have found no basis for apportioning constant costs except by a prorate of tons or ton-miles—a method vulnerable to criticism as arbitrary. The defendants here direct that criticism to the studies of the complainants and the mid-western lines. In so doing they inferentially recognize a somewhat restricted field for cost evidence in cases of this kind, as indicated by the following observation of their principal cost witness:

> There is necessarily more to divisions than a showing of the comparative costs of the service performed, no matter how effectively this latter task may be performed. Section 15(6) of the Interstate Commerce Act refers to the amount of revenues required to pay respective operating expenses, taxes, and fair return,

> including total carrier financial needs, carrier credit and the burden of meeting the necessary constant costs, the passenger deficits and return on investment. The composition of each carrier's traffic, the distribution of the burden among all traffic carried, and the financial dependence of the respective carrier upon the traffic in question are vital factors here to be weighed. It is plain that no single formula can be used to fix fair divisions under all circumstances.

[fol. 856] Thus the constant costs are shifted into the broad outlying fringes of the problem without any specific suggestion as to how those costs should be here dealt with except upon general judgment. We agree with the statement above-quoted to the effect that cost studies do not furnish the final solution to the problem and this seems to be an added reason for not attempting meticulously to unravel the tangled skein of controversy surrounding the studies here.

The essential question to be decided is whether there are differences in the general levels of railroad costs prevailing in eastern territory, mountain-Pacific territory, and the remainder of western territory, which affect the expense attributable to movements of freight between those territories. We are convinced that the defendants' cost studies understate the costs in official and midwestern territories, although the amount of the understatement cannot be approximated from the studies of the eastern and midwestern lines and other data of record.

The issues in these cases are similar in some respects to the questions before the Commission in *Class Rates, Mountain-Pacific Territory,* 296 I.C.C. 555. Its conclusions concerning the cost evidence presented by the participating carriers and others, including its own cost finding section, are quoted in the note.[11]

In that report the Commission made the following formal finding based on evidence, (p. 655-6) most of which did not go beyond the year 1954:

> We further find that economic conditions, as well as the transportation and operating conditions of the railroads, have substantially improved in mountain-Pacific territory within the last 20 years, and, while other areas of the United States have undergone a similar trend, the growth and progress in mountain-Pacific territory have been more pronounced than in the areas east of the Rocky Mountains. Reference, in this connection, is made to our findings herein with respect to the relative costs of railroad transportation within, to, and from mountain-Pacific territory as compared with those in other territories, and as compared with the United States as a whole, which are more fully and particularly set forth in the section of this report entitled "Cost Studies." The differences in costs as between mountain-Pacific territory and other territories are not uniform in the various mileage blocks or for different classes of cars used in transportation service. As shown by the cost studies, however, the differences in costs no longer justify maintenance of the existing differences in class rates as between mountain-Pacific territory and 28300 territory.

Although the Commission in that report made no definite finding concerning the approximate differences in territorial cost, if any, it approved the interterritorial class rates proposed by the transcontinental lines, which were about 9.5 percent higher on the average than those which would have been produced by the 28300 scale to and from eastern territory and about 12.5 percent higher than those to and from other sections of western territory.

That action tends to support the view that the higher basis of class rates prescribed was at least partly in recognition of differences in costs and other conditions affecting the transcontinental lines, and we have taken that action [fol. 857] into account among other considerations in our recommendations. Likewise we have noted the finding in the final sentence above-quoted, which consistently with

the cost evidence here of record, justifies the same conclusion as to divisions.

REVENUE NEEDS

The report in *Class Rates, Mountain-Pacific Territory, supra,* contains a detailed discussion of the growth and economic development of mountain-Pacific territory and its relation in those respects to other territories. To a considerable extent that discussion was based on evidence presented by the mountain-Pacific State commissions, which were there supporting a reduction in the class rates but are here aligned with the defendants in arguing for an increase in their divisions. Some of that evidence was also incorporated in the present record.

On p. 583 of that report is a table showing increases in population of the States in mountain-Pacific territory from 1920 to 1952. During that period the total increase for those States was 134.7 percent compared with 47.4 percent for the United States as a whole. Recently released preliminary figures for the 1960 census indicate that between 1920 and 1960 the population of the mountain-Pacific States increased 202 percent, the increase for the entire country in the same period being 70 percent.

The table above referred to was the subject of the following paragraph, to which have been added bracketed interpolations to bring it up to date:

"The foregoing table shows substantial gains in population for (most) [all] of the States in mountain-Pacific territory, but the major portion of the increase occurred in the Pacific Coast States, particularly in California where the population has (nearly doubled) [increased 125 percent] since 1940. The percentage of increase in Arizona leads all the other States with the exception of California. The phenomenal growth of the 11 western States since 1940 is largely due to activities in connection with World War II. The expected postwar decline in population did not materialize for manufacturing, and the demand for con-

sumer goods which expanded under the war economy has continued in an upward trend rather than a downward trend to meet the needs of the postwar economy."

In 1890, when the divisions here under consideration had begun to conform to their present pattern, the population of the mountain-Pacific States was 3.102 million, 5 percent of the total of the entire country. The present population of the same States, 26.9 million, is 15 percent of the total. The shifts in population and consequent economic changes have also had marked effects on the fortunes of the railroads.

After the end of World War I temporary unsettling influences affected the railroads in 1919-1922. Accordingly the relatively prosperous period from 1923 to 1930, inclusive, before they began to suffer acutely from the depression of the 'thirties', affords a fair basis of comparison with the post-World War II period since 1945. The average annual freight traffic of the American railroads, measured by revenue ton-miles, was about 44 percent greater in 1946-1958 than it was in 1923-1930, but the increase was by no means uniform, as shown in the following statement:

[fol. 858]

	Revenue Ton-Miles			
	1923-1930		1946-1958	
	Annual Average (Millions)	Percent of Total	Annual Average (Millions)	Percent of Total
Eastern District	176,591	42.1	197,024	32.6
Pocahontas Region	40,807	9.8	57,142	9.5
Western District	144,215	34.4	263,674	43.6
Southern Region	57,377	13.7	86,520	14.3
	418,990	100.0	604,360	100.0
Transcontinental Group	58,553	14.0	130,889	21.7

Some features of the foregoing figures should be emphasized, notably the increase of nearly 124 percent for the transcontinental group. The increase for the western district other than that group was 55 percent, somewhat more than the southern increase of 51 percent. The increase for the eastern and Pocahontas lines was only 12 percent and was responsible for the striking decline of their share of the total from 51.9 percent in 1923-1930 to 42.1 percent in 1946-1958, putting them below the western district.

The following statement is a similar comparison of freight revenue:

Freight Revenue

	1923-1930		1946-1958	
	Annual Average (Thousands)	Percent of Total	Annual Average (Thousands)	Percent of Total
Eastern District	$1,949,672	42.6	$2,887,164	36.0
Pocahontas Region	281,911	6.2	548,222	6.8
Western District	1,718,330	37.6	3,447,226	43.0
Southern Region	621,816	13.6	1,143,313	14.2
	$4,571,729	100.0	$8,025,925	100.0
Transcontinental group	$ 712,896	15.6	$1,730,525	21.6

The increase in the figure for the transcontinental group was 142 percent, compared with the overall average increase of 76 percent. For the western district other than the transcontinental group the average increase was 70 percent.

[fol. 859] Net railway operating income is compared in the following statement:

Net Railway Operating Income

	1923-1930 Annual Average (Thousands)	1923-1930 Percent of Total	1946-1958 Annual Average (Thousands)	1946-1958 Percent of Total
Eastern District	$ 446,080	41.3	$268,618	29.1
Pocahontas Region	86,999	8.1	99,780	10.7
Western District	405,513	37.6	403,406	43.7
Southern Region	140,332	13.0	152,354	16.5
	$1,078,924	100.0	$924,158	100.0
Transcontinental group	198,966	18.4	203,160	21.9

The most significant feature of the foregoing statement is the reduction of 31 percent for the carriers in official territory contrasted with the overall reduction of 14 percent.

The three comparative statements last above shown indicate clearly the inferior position of the railroads in official territory as freight carriers, compared with the western district since World War II. In 1923-1930, the annual average ton-miles of the official territory lines exceeded those of the western district by 51 percent; in 1946-1958 the official average was 4 percent lower than the western. The official lines in 1923-1930 had 30 percent more freight revenue than the western district; they had 3/10 of one percent less in 1946-1958. The net railway operating income of the official lines in 1923-1930 was 31 percent greater than that of the western district; in 1946-1958 it was 9 percent less.

The three statements also show the growing importance of the transcontinental lines. In 1923-1930 they accounted for 40.6 percent of the ton-miles of the western district; their percentage in 1946-1958 was 49.6. Their freight revenue in 1923-1930 was 41.5 percent of the total for the western district; this percentage increased to 50.2 in 1946-1958. The transcontinental lines' percentage of the total net railway operating income of the western district, however, increased only from 49 percent in 1923-1930 to 50 percent in 1946-1958, for reasons discussed *infra*.

Comparative rates of return on investment represented by the earnings above shown will now be considered.

The defendants say that such comparisons should be centered on "1955 and 1956, the most recent years of normal business activity and also for 1957, a year influenced by the recent recession." These years were 3 of the only 4 years between 1946 and 1958 in which the net railway operating income of the eastern roads exceeded that of the roads in western district, 1953 being the other. Conse- [fol. 860] quently in these 3 years the eastern figure exceeded the western by about 7 percent. The average rate of return for the eastern district and the Pocahontas region in this period was 3.82 percent and for the western district 3.50 percent. In the 13 years, 1946-1958, as a whole, eastern net railway operating income was 9 percent lower than the western. (The effect of differing passenger deficits on this comparison will be pointed out later.)

Whether 1955, 1956, and 1957 may be considered "normal" years is a matter of opinion as to which economists might well differ. They were clearly not representative years for the 1950 decade, however, as commonly accepted business indices show them to have been among the highest in 1951-59. Certainly they were not representative for comparing earnings of the eastern and western railroads.

Until about 15 years ago the only available method of computing rates of return was to divide net railway operating income by investment in railway property as recorded in the carriers' accounts. To compare current rates of return with those for years before 1945 it is still necessary to use this method. In the following statement average

rates of return for the principal railroad groups in the period 1946-1958 are compared with those in 1923-1930, the investment bases being recorded investment in road and equipment, materials and supplies, and cash, less accrued depreciation and amortization:

Rates of Return on Book Investment

	1923-1930 Percent	1946-1958 Percent
Eastern District	4.97	2.81
Pocahontas Region	7.27	6.35
Eastern District and Pocahontas Region	5.26	3.30
Southern Region	4.63	4.47
Western District	4.23	3.68
Transcontinental group	4.58	3.86
Western District except Transcontinental group	3.94	3.50
Midwestern lines (complainants) in Sub No. 1)	—	3.49

In recent years comparisons of this kind have also been based on the elements of value determined by use of the Commission's valuation data. For example, at pages 612-3 of the report in *Class Rates, Mountain-Pacific Territory, supra,* both methods were used in showing the following average rates of return for 1946-1954:

[fol. 861]

Rates of Return

	Net Investment Percent	ICC valuation Ex Parte No. 175 Percent
Eastern District (including Pocahontas Region)	3.31	3.46
Western District	3.83	4.38

The difference is due principally to the discrepancy between recorded investment and valuation data for the transcontinental lines. The latter, therefore, urge strongly that in comparing rates of return their book figures only should be used, while the complainants and the midwestern lines favor the use of the elements of value. The different results are shown in the following statement:

Average rates of return, 1947-1958

	Book Investment Percent	Elements of Value Percent
Eastern District	2.90	2.98
Eastern District and Pocahontas Region	3.41	3.56
Midwestern lines	3.54	3.69
Transcontinental group	3.92	4.65
Western District	3.69	4.19

The disagreement on this point reflects a controversy which has existed for 15 years or more and hinges on the question whether the elements of value or the railroad's book investment figures more nearly show present values of their property for the purpose of administering the Interstate Commerce Act. The matter is considered to be of particular importance by the transcontinental railroads, whose book investment figures are farthest out of line with the elements of value. As of 1957, the excess in the recorded investment of the defendants, was about 10.4 percent on the average. For the Southern Pacific, Northern Pacific, and Union Pacific, however, the differences were greater.

On behalf of these defendants it is asserted that they were "pioneer railroads," and that their cost of reproduction as found by the Commission's Bureau of Valuation assumed the use of facilities which did not exist at the time of original construction. The evidence offered in support of this view we believe, is insufficient to disclose infirmities

in the valuation process and certainly insufficient to show that the book figures of the defendants are unimpeachable.

The same question was considered in the Commission's report in *New Automobiles in Interstate Commerce, supra,* which the defendants to a considerable extent have relied on here. There our section of cost finding used the elements of value. On page 524 of the report, it was pointed out that "all railroads declined to accept the rate-making values furnished by the Bureau of Valuation," but the Commission was not impressed by that attitude, stating that "all of the elements of value which the act requires shall be considered were taken into account by the Bureau of Valuation."

[fol. 862] In 1948 the then director of the Commission's Bureau of Accounts and Cost Finding proposed an accounting order to require rail carriers to enter on their books of account the estimated original cost of their transportation property as developed by the Commission's Bureau of Valuation in substitution for the recorded cost. We believe that the position of the director was sound. (Apparently he saw no reason at that time for making any exception of "pioneer roads.") Although his recommendation was not acted upon, we understand that the subject is not closed, and in our opinion it would not be desirable for the Commission, on the facts here presented, to voice acceptance of the defendants' contention with respect to their recorded investment.

In our judgment, controlling weight should be given the showing based on elements of value consistently with the views expressed by the Commission in other divisions cases.[12]

Another contention of the defendants is that "the data of record overstate the true costs and understate the real earnings of the New York Central and the Chicago & North Western because they reflect acknowledged inefficiencies of their prior managements." In 1954 there was a change in the management of the New York Central after a heated and widely-publicized proxy fight. About 2 years later, under somewhat different circumstances, the executive control of the North Western also changed hands.

The defendants presented a considerable number of statements in speeches, reports to stockholders, talks to security analysts, press releases, and testimony in administrative proceedings, in which the new executives criticized previously existing conditions on these railroads and commented unfavorably on the managerial capabilities of their predecessors. According to the defendants, the present officers, marked by "skill and energy, ... have undertaken vigorous programs for the rehabilitation of their properties, but the programs which will reduce costs and improve earnings have of necessity inflated operating expenses for recent years." They therefore urge that "financial comparisons should exclude the temporarily depressed earnings of those two roads." The omission of the New York Central would raise the average rate of return of the eastern railroads in 1946-1958, based on book values previously shown in this report as 3.30 percent, to 3.57 percent, and the omission of the North Western similarly would increase the rate of return for the western district from 3.68 percent to 3.80 percent.

The Commission is required to give "due consideration, among other things, to the efficiency with which the carriers concerned are operated," but in the nature of things such consideration presents great difficulty in assigning a definite weight to this element in appraising either cost or revenue need. We are inclined to discount the importance of the criticism of past managements of the New York Central and the North Western in the evidence before us as proof of past inefficiency. Likewise we point out that the success of the new managements still remains to be demonstrated by future performance. (The defendants' predictions of a bright future for these two railroads were made before the 1959 statistics became available.)

The problems of the New York Central and the Chicago & North Western in the past 15 years have been numerous and varied, and there are points of similarity in the situations of the two companies. Both have been dependent on passenger traffic for a greater share of their gross revenue

than other railroads in their respective territories, and [fol. 863] both have had acute commutation problems. As their passenger traffic has become increasingly more costly, their freight traffic has declined to a greater extent than that of other railroads. Even if it be conceded that there may have been some inefficiency in their past operations, that circumstance would not bar the possibility that insufficient freight revenue, due in part to inadequate divisions, was to some extent a contributing cause.

For a proper comparison of rates of return the defendants would have us find that "consideration of the acquisition adjustment account is necessary to reflect the investment in road and equipment property of the carriers party to this proceeding." They contend that "the disregard of the acquisition account sought by the midwestern lines, is an effort unlawfully to increase the investment of the reorganized carriers."

The acquisition adjustment is an assets account in the balance sheets of carriers which have undergone financial reorganization and was prescribed in *Chicago G.W.R. Co. Reorganization,* 247 I.C.C. 193 (1941). The reasons for the use of the account are fully stated in that report and need not be repeated here.

The practical significance of the point raised by the defendants is indicated in the following excerpt from their brief:

> Failure to consider acquisition adjustment reduces the rate of return of the Midwestern roads by about 3/10ths of a percentage point, as compared to about 1/10th of a percentage point for the Mountain-Pacific roads, thereby changing rate of return comparisons by some 2/10th of a percentage point in the interest of the Midwestern lines in this divisions proceeding. The Midwestern lines' disregard of the acquisition adjustment account is an effort to reverse the Commission and judicial action determining the investment of the reorganized roads and, specifically, to reverse the Com-

mission's 1941 decision [above cited] establishing the investment accounts for reorganized roads.

By section 15(6) of the Interstate Commerce Act, the Commission in prescribing divisions is required to give due consideration, among other things, to the amount of revenue required to pay a "fair return on their railway property held for and used in the service of transportation." The defendants' contention is in substance that the value of such property is net investment therein as shown in the carriers' accounts determined by deduction of the acquisition adjustment in case of reorganized railroads. It appears to us clear from the report above cited that the Commission actually undertook to dispel any such impression when it prescribed the acquisition adjustment. At page 196 of that report it said:

> In the accounting classifications which we have prescribed for the carriers subject to our jurisdiction, investment in physical property is not stated on the basis of value but on the basis of cost. The amount shown as such investment in the balance sheet does not purport to reflect the value of the property in either sense above indicated, [i.e., "value in the strict economic meaning of the word" and "value for rate-making purposes"] but only its cost to the accounting carrier.

[fol. 864] In our opinion the fair return mentioned in section 15(6) may and should properly be based on "value for rate-making." This view is consistent with the Commission's 1941 decision rather than inconsistent, as the defendants argue.

It is generally agreed that comparisons of net railway operating income alone are not entirely reliable in judging the significance of rates of return on investment because of certain distortions in the incidence of the Federal income tax. Of principal importance is the fact that that tax applies to nonoperating income, known as "other income", as well as revenue from railway operations. The

defendants have larger proportions of other income than the other contending groups. Another complication is due to the availability of income-tax savings from accelerated amortization of cost of defense projects completed before 1956. Thus Federal income taxes were temporarily deferred for five years after completion of such projects through higher-than-normal tax credits, and in all probability the tax burden will be increased correspondingly for the remaining life of the property. The western roads principally received defense-project certifications, which thus indirectly tended to overstate their net income. Adjustments in reported net railway operating income to allow for these distortions can readily be made and are shown in the record. In the following statement average rates of return for 1951-1958 based on adjusted and unadjusted net railway operating income applied to book investment bases are shown:

Average Rates of Return on Book Investment, 1951-1958

	Unadjusted n.r.o.i. Percent	Adjusted n.r.o.i. Percent
Eastern District and Pocahontas Region	3.47	3.26
Midwestern Lines	3.54	3.11
Transcontinental lines	3.83	3.70

In comparing net railway operating income and rates of return based thereon differences in respect of the passenger deficit, which have an important bearing on such comparisons, must also be kept in mind. Because of the serious decline of the traffic of the eastern carriers in the past ten years, the accompanying passenger deficit has undoubtedly created a serious problem for those railroads. Contrary to popular impression, however, in this period the passenger deficit has been larger in the West than in the East, and the eastern carriers have done better in reducing their passenger deficits than the western lines.

The record contains statistics for the years 1950-1958 showing annual passenger deficits and freight net railway operating income for the larger railroads in all territories. It is desirable to take official notice of corresponding published figures for the earlier years of 1948 and 1949 as well as of those for 1959 now available and also to take official notice of total amounts for the eastern district (including the Pocahontas region) and the western district. A comparison of the figures for 1948, with those of later years, is shown below. The use of 1948 as a base is appropriate because in that year the total passenger deficit of all railroads reached half a billion dollars for the first time in railroad history.
[fol. 865]

Passenger Deficits (Thousands)[13]

Year	Eastern District and Pocahontas Region	Western District	Transcontinental lines (AT&SF, D&RGW, GN, NP, SP, UP)
1948	$252,145	$234,625	$107,492
1949	245,780	290,797	139,332
1950	214,330	229,893	110,977
1951	299,915	295,839	151,621
1952	273,666	286,534	146,894
1953	273,556	338,403	181,202
1954	232,512	345,800	193,202
1955	232,233	321,350	172,546
1956	255,411	347,002	189,944
1957	271,336	349,352	193,310
1958	206,391	311,883	170,400
1959	177,716	287,594	159,189
Average 1949-1959	$243,895	$309,494	$164,419

Several aspects of this showing should be noted. The eastern average for 1949-59 was 3 percent lower than the 1948 deficit, and in 1959 it was 30 percent lower than it was in 1948. The 11-year average for the western district was about 32 percent higher than the 1948 figure, and the western deficit in 1959 was 23 percent higher than it was in 1948. The unfavorable western showing is accentuated by the inclusion of the transcontinental lines. Their average annual deficit for 1949-59 was nearly 53 percent higher than that of 1948, and even after the slight reduction in 1959 it remained 48 percent higher. The passenger deficit for the western district in 1959, excluding the transcontinental lines, would have been only about one percent higher than the 1948 deficit. In 1948 the deficit of the transcontinental lines accounted for 19 percent of the total of all American railroads, and that percentage rose to 29 percent in 1959.[14]

If the rail carriers in the western district had been able to hold their average annual passenger deficit in 1949-1959 to a figure 3 percent less than their 1948 deficit, their revenue saving would have been nearly $82 million per year. The annual saving of the transcontinental railroads similarly estimated would have been more than $60 million per year.[15]

The complementary comparison of freight net railway operating income in the next statement is pertinent.

Net Railway Operating Income—Freight Service (Thousands)[16]

Year	Eastern District and Pocahontas Region	Western District	Transcontinental Lines
1948	$680,231	$668,836	$313,939
1949	539,970	606,517	288,162
1950	604,012	710,717	344,495
1951	681,904	699,651	356,206
1952	711,743	743,865	360,612
1953	737,314	789,303	388,312
1954	566,320	724,517	383,044
1955	713,002	771,050	404,292
1956	721,294	764,830	402,826
1957	656,067	731,554	392,175
1958	440,770	700,285	378,417
1959	439,634	636,190	352,241
Average 1949-1959	$619,275	$716,225	$368,253

[fol. 866] The foregoing statement shows that the eastern average for 1949-59 was about 9 percent lower than the figure for 1948, and the 1959 income was 35 percent lower than that of 1948. On the other hand, the western average for 1949-1959 was 7 percent higher than the 1948 figure, and the decline in 1959 was only 5 percent. In 1949-59 the transcontinental lines had an average annual gain of 17 percent over 1948, and their percentage of gain in 1959 was 12 percent. Without the transcontinental lines the western district in 1959 would have had a 20-percent reduction below 1948.

In the 12 years from 1948 to 1959 the western district had average freight net railway operating income of $712,276,000 which was 14 percent greater than the eastern average of $624,355,000. The difference in dollars was $87,921,000. This was a considerably greater spread than that between the average annual net railway operating income of the two groups from all services in the same period, $378,239,000 for the eastern lines and $408,554,000 for the western district, amounting to $30,315,000 or 8 percent.

The defendants say in their brief:

> The traffic available to support the mountain-Pacific roads is very different from the traffic upon which the Midwestern and Eastern lines depend for their revenues. The severely depressed rates and unusual character of that traffic pose the greatest threat to the ability of the Mountain-Pacific lines to maintain even their present low level of earnings and return to their owners.

Because of "hold downs" affecting their rates which have resulted from the general rate increases since World War II, one of the defendants' witnesses, a Union Pacific executive, testifying in 1956, stated that "rate action which has been designed broadly, and generally on a national basis, to offset increases in costs, has fallen far short of doing so in respect to the principal transcontinental traffic because of its highly competitive character." In the same vein he went on to say:

> . . . just in the degree that the mountain-Pacific roads' reliance on traffic subject to this inherent disability is greater than that of other groups of roads, the persistent decline in our rate of return is more serious than that of other lines. . . . The competitive factors inherent in the traffic we handle operate to impose holddowns in the rate advances required by each round of wage increases. As this pattern is projected into

> the future * * * the position of the Union Pacific and other mountain-Pacific roads dependent on the long haul holddown traffic will continue to deteriorate relative to the roads relying on other traffic for the greater part of their revenues . . . the public has not been adequately aware of the Union Pacific's extremely unfavorable position as a railroad. Our eastern and midwestern friends have perhaps been more energetic in advertising their difficulties.

There has been no deterioration of the kind above mentioned. It has already been shown that the financial position of the mountain-Pacific lines as freight carriers in the post-war period as a whole has been better than that of either the eastern or the other western lines. This has also been true since 1956, when the testimony above quoted was given. The average freight net railway operating income of the transcontinental lines in 1957-1959, was only 7 percent less than it was in 1956, and the Union Pacific's decline [fol. 867] was slightly more than two percent. On the other hand, the other western lines had a reduction of 13 percent, and the average annual freight net railway operating income of the official lines in 1957-1959 was 22 percent lower than it was in 1956.

The comparisons of freight net railway operating income and passenger deficits also have a bearing on the assertion of the defendants that "the increased investment required in serving the growing mountain-Pacific territory has produced no return for the owners of the mountain-Pacific roads." This alleged deprivation results from excessive passenger deficits of those roads, as will now be explained.

For example, it is shown that in 1955 the Union Pacific had net railway operating income of $43.7 million and $44.1 million in 1950, a reduction of one percent, although its net investment in the same period had increased 21 percent. Its freight net railway operating income, however, increased from $74.8 million in 1950 to $90.3 million in 1955, an increase of 21 percent. For the 9 years 1951-1959 its

average annual increase in such income has been 10 percent over 1950. This increase has not been reflected in net railway operating income from all services, however, for the reason that in 1951-1959 the Union Pacific had an average passenger deficit of $45.4 million per year, 50 percent greater than its deficit in 1950.

Similarly the defendants say that "in the 5-year period 1951-1955 the mountain-Pacific roads found it necessary to increase their net investment in transportation property by $800 million * * * but this increase in investment produced not one penny of earnings." Defendants say further by way of explanation:

> The net railway operating income of the mountain-Pacific rail group since 1950 has never equalled the 1950 figure. In effect, this group of carriers had yet to receive any return on the added $801 million investment in rail plant which it has made since the beginning of 1951.

Between 1951 and 1955 inclusive, the major mountain-Pacific railroads (AT&SF, GN, NP, SP, and UP) increased their net investment by $731 million, and the improved facilities were undoubtedly helpful to them in handling a steadily growing volume of traffic, which, measured by revenue ton-miles in each year since 1950, has shown an average increase over that year's volume of 10 percent and has produced freight net railway operating income annually averaging 9.5 percent above that of 1950. Their decline in net railway operating income from all services since 1950, reflects the fact that since that time they have had an aggregate passenger deficit of $1.5 billion, an annual average of $168.4 million, 58 percent greater than their deficit in 1950.

The intervening State Commissions share the defendants' concern as to whether those railroads can obtain necessary funds to increase their facilities to the extent necessary to keep pace with the expanding economy of the mountain-

Pacific States. One of the interveners' briefs has the following to say on this point:

> In spite of the pressing need for additional investment in equipment and transportation facilities, the mountain-Pacific carriers cannot look to rate increases to provide increased earnings but instead must face further rate reductions. Where then is the money necessary to provide additional facilities, and to maintain [fol. 868] the earnings of the Mountain-Pacific carriers to come from? With these carriers dependent for over half of their freight revenues on these transcontinental divisions, it seems only fair that the Midwestern and Eastern connections, who participate in the transcontinental traffic without having had to make the necessary capital investments at anything approaching the same rate, should be called upon in this divisions proceeding to provide at least a modest increase in the transcontinental divisions accruing to Mountain-Pacific lines.

It has already been pointed out in this report that the various changes in the country's freight-rate structure in the past 15 years have not prevented the mountain-Pacific railroads from attaining a greater degree of prosperity as freight carriers than the eastern and midwestern lines. The mountain-Pacific lines, however, are losing relatively much more money than the others on their passenger traffic, and we see no reason for offsetting those losses by increases in their revenue from transcontinental freight. The obvious answer to the question stated in the foregoing quotation is that a reduction in the passenger deficit of the mountain-Pacific lines, which would seem to be imperative sooner or later, should help materially in furnishing funds for additions and betterments. The interveners are in a position to assist in such a course by taking a sympathetic attitude toward discontinuance of unprofitable passenger service. The American railroads other than the defendants

in 1959 had a total passenger deficit 15 percent lower than they had in 1948. If the defendants had been able to do as well, they would have had a saving of $67.8 million in 1959.

The defendants point out that in 1956, the eastern lines' net railway operating income from all services was 22 percent higher than it was in 1951, while the increase for the mountain-Pacific lines in the same period was only 4 percent. (The difference between the two groups in 1956 in respect of these figures was unusually wide.) Here again the differing passenger deficits must not be disregarded. A comparison of freight net railway operating income of the two groups in 1956 and 1951 shows an increase of 6 percent for the eastern lines and 13 percent for the transcontinental railroads.

Upon the facts relating to revenue need discussed on preceding pages it is our conclusion that the eastern railroads are in a much less advantageous situation as freight carriers than those in the western district. The most favorable comparison from the standpoint of the western lines, we believe, is the showing that the average return of the eastern district and Pocahontas region in 1946-1958, based on net railway operating income from all services adjusted for income tax differences as before explained, related to book investment was 3.26 percent, compared with 3.34 percent for the midwestern group and 3.89 percent for the transcontinental defendants. If the elements of value are used as the investment base, the percentages become 3.40 for the eastern lines, 3.49 for the midwestern group, and 4.64 for the defendants. A more illuminating comparison for the purpose of these cases would be one using freight net railway operating income, and undoubtedly it would show a still greater degree of financial superiority for the western lines.

But even more significant than a comparison of rates of return is the post-war trend of declining freight traffic of the eastern railroads shown in this record. Their average annual ton-miles for the period 1947-1959, 250.6

million, have been 5 percent lower than the number in [fol. 869] 1946, 263.6 million. In only 4 of those years, 1947, 1948, 1951 and 1956, has their traffic measured by revenue ton-miles, exceeded that of 1946. The railroads in the western district, on the other hand, have had an average of 265.6 million ton-miles per year, compared with 244.2 million in 1946, an increase of 9 percent. In only one year since 1946, namely 1949, has the western district failed to show an increase over 1946. Throughout railroad history prior to 1949, the western district was far behind the eastern district and Pocahontas region in comparisons of revenue ton-miles, but that year marked the turning point. In each year since 1948 the western district has led the East by an annual average of 9 percent. No developments are in sight which would point to a reversal of these trends.

We turn now to the assertion of the midwestern lines that their revenue needs "are greater than those of the opposing eastern and transcontinental roads." They principally rely on statistics for 1957, which they consider "the most accurately representative recent year." In 1957 their net railway operating income, $108.85 million, was the lowest of any year since 1946 and was 17 percent lower than the average of $130.6 million for 1946-1958. This 1957 figure was lower by $101 million than the net railway operating income of transcontinental roads and lower by $276 million than that of the official lines. The respective average differences in the 13-year period were $78.7 million and $230 million. With adjustment for differences in income tax before described the midwestern lines show that their rate of return on elements of value in 1957 was 2.56 percent, compared with 3.17 percent for the official lines and 3.53 percent for the transcontinental group. The average rate of return for the midwestern lines in 1946-1958 was 3.49 percent.

In considering the earnings of the midwestern lines, their passenger deficits must also be taken into account. Their performance has been somewhat better in this respect than that of the transcontinental lines, but inferior to that of the

eastern railroads. The statement below shows net railway operating income from freight service and passenger deficits of the IC, GM&O, C&NW, CRI&P, MKT, MoPac, StL-SF, CB&Q, and CMSTP&P for the years indicated.

Midwestern Lines[17]

Year	Freight Net Railway Operating Income (000)		Passenger Deficit (000)
1948	$267,215		$100,927
1949	243,47[illegible]		124,009
1950	289,037		96,926
1951	274,964		121,047
1952	297,479		116,126
1953	304,298		130,797
1954	275,569		130,938
1955	286,316		125,264
1956	302,428		143,851
1957	280,223		147,797
1958	276,789		134,823
1959	241,047		120,055
	$279,239	Averages 1949-1959	$126,512

The midwestern lines' passenger deficit was 18 percent of the total for all class I railroads in 1948 and 22 percent in 1959. It is clear that they too have a potential source of increased revenue by further reductions in this deficit.

[fol. 870] Those lines have shared in the post-war expansion of railroad freight traffic in the western district before pointed out. In only 3 years of the 1946-1958 period, namely 1949, 1954, and 1958, did their ton-miles fall short of the number of 1946. Their over-all average increase has been about 3 percent, compared with 13 percent for the transcontinental lines and 5 percent for the western district other than the latter lines.

Upon all the evidence relating to revenue need it is our view that the midwestern lines rank below the transcontinental railroads in earning power as judged by statistics for the post-war period and that their prospects for sustained or increased freight income are less promising than those of the defendant transcontinental railroads. At the same time we believe that as a group, they must be judged to be in a considerably more favorable condition than the eastern railroads. That view is counter to the object of the midwestern lines stated in their brief as follows:

> The revenue effect of the proposal of the midwestern complainants, based on their one percent traffic study for 1953-1955, would be increases in revenue of 23.62 percent for the Midwestern lines and 4.78 percent for the Eastern lines, and reduction in revenue of 9.19 percent for the Transcontinental lines and 1.67 percent for the Southern lines. * * * the revenue results would be increases of approximately $38 million per year for the Midwestern lines and $4 million per year for the Eastern lines, and reductions of approximately $42 million per year for the Transcontinental lines and $3,300 for the Southern lines.

No less fanciful in our opinion is the finding requested by the defendants that "an increase in the present divisions of the mountain-Pacific railroads of not less than 10 percent is justified" for the reason as colorfully stated in 1956 by their principal witness that "the mountain-Pacific group of roads has the poorest financial position of any of the groups participating in the transcontinental traffic. * * * the 'low man' on the rate of return 'totem pole.'"

Conclusions

The proposal of the defendants and their intervening allies that the divisions of those carriers be increased at least 10 percent ostensibly is premised on a contention that, as the transcontinental traffic accounts for some 50 percent

of their revenue, that traffic should in large measure afford (1) satisfactory dividends to stockholders, (2) a depressed rate structure which would continue to give mountain-Pacific producers access to eastern markets, (3) funds for the financing of improved facilities necessary to serve the growing West, and (4) inferentially a passenger deficit amounting to nearly $160 million per year. To require an increase in their divisions to further these objectives seems to us so palpably unfair to the midwestern and eastern lines that we are inclined to regard the proposal as a defensive maneuver in the nature of a diversion (in the military sense of the word).

To increase the defendants' divisions 10 percent would have the effect of throwing upon the eastern and midwestern lines most, and in some cases all, of the burden of absorbing the reductions in the interterritorial class rates to and from mountain-Pacific territory approved by the Commission 5 years ago based principally on improved economic and transportation conditions in that territory. This may be [fol. 871] shown by reference to p. 572 of the report in *Class Rates, Mountain-Pacific Territory, supra.* The first-class rate from New York City to Seattle was reduced from $11.72 to $9.38. The present division of the New York-Seattle rates west of the Twin Cities or Council Bluffs is 60.5 percent, which increased 10 percent as proposed would become 66.55 percent. Applying these two percentages to the respective rates before stated would have given the transcontinental lines a reduction of 85 cents (12 percent), and the connecting lines a reduction of $1.49 (32 Percent).

There can be no doubt that transportation and economic conditions affecting the eastern and western railroads today are far different from those which prevailed in the half century from about 1880 to 1930 when the divisions of the transcontinental rates were crystalized in their present form. In the past 10 years it has become clear that the eastern railroads no longer have available to them the profitable volume of freight originating and terminating within

their own territorial borders which before World War II caused them to be generally regarded as the strongest group of all American railroads. Accordingly they have become increasingly dependent on interterritorial traffic, which has grown in importance and stability. About 7 years ago the Commission found them to be entitled to higher divisions of their interterritorial rates to and from the South and Southwest. Their opponents at that time contended that the troubles of the eastern lines were temporary and would disappear when they realized the full benefits of greater use of diesel locomotives and other improvements. Those predictions were not borne out by later developments, and we are therefore skeptical concerning somewhat similar predictions which have been made in the instant proceedings. In our opinion, under the duty of the Commission to consider the requirement of the public interest that all essential parts of the transportation system be maintained, so far as possible, in effective working condition there should be a moderate general increase in the divisions of the eastern railroads.

As between the transcontinental lines and the other western railroads the financial disparity is less marked, but the time is opportune for a number of adjustments of individual divisions in the interest of "justice merely as between the parties." [19] Some of the more important divisions, we believe, are clearly unfair to the midwestern lines. In other instances it is the divisions of the transcontinental lines which appear to be too low, as indicated by the fact that they would be increased even under the proposal of the midwestern lines.

In Sub No. 1 principal attention has been centered on the divisions of rates to and from midwest-east territory, which are of outstanding importance. These were the subject of the Commission's 1934 decision before referred to, which was an important victory for the transcontinental lines, continuing the divisions fixed by the 1925 agreement for some 25 years longer down to date. Here too, changes have occurred.

In the 1934 report the Commission emphasized the fact that "the transcontinental traffic is unevenly balanced as to direction," pointing out that "eastbound it is in general more than 3.5 times as heavy as westbound." (p. 320) The 1953 traffic tests of the defendants show a movement of 993,141 cars eastbound and 664,035 cars westbound, the former figure being less than 1.5 times the latter.

The present divisions between Missouri River junctions and Chicago and St. Louis appear to be too low even in the light of the defendants' own cost evidence, upon which, as they say, "cost scales were then constructed to measure the [fol. 872] cost of handling the transcontinental traffic in the respective territories." The average distance between Council Bluffs and the 4 Pacific ports is 1,778 miles, and the Chicago-Council Bluffs distance is 473 miles. The costs shown in the defendants' 1956 cost scales are 22.34 cents per 100 pounds for 500 miles in midwestern territory and 87.15 cents per 100 pounds for 1,800 miles in mountain-Pacific territory. Using these costs for prorating gives 20 percent for the midwestern movement and 80 percent for the mountain-Pacific haul in contrast to the present divisions of 16.5 and 83.5 percent. Likewise the scales would support an increase in the Kansas City-St. Louis division from 12.1 percent to 15 percent. For rates between Chicago and Boise the cost scales would support an increase in the division east of Council Bluffs from 16.5 percent to 25 percent.

Under the proposal of the defendants for an increase of at least 10 percent in their divisions the Chicago-Council Bluffs division would be reduced from 16.5 percent to 8.15 percent and the Kansas City-St. Louis division now 12.1 percent would fall to 3.31 percent. These figures underline the gross inequality in the present divisions, which would be magnified by the 10-percent proposal.

A historical explanation of this situation may be found in the circumstance that nowhere else in this country is there such highly developed rail-carrier competition as that

between the Missouri River cities and the Twin Cities, on the one hand, and Chicago and St. Louis, on the other, where some half dozen rail routes are active seekers of traffic. It is significant that for one reason or another, never before have the western trunk lines apparently felt free to join in a united effort to obtain higher divisions for their service in this territory. Even the CB&Q, seemingly anticipating the possibility of the success of the present effort, has not been deterred by its corporate ties from filing its separate complaint.

Specific Divisions vs. Scales—Throughout these proceedings the parties have considered it likely that any prescribed readjustments would be based on the use of divisional scales, popularly known as integer scales, which have been utilized in some other interterritorial divisions decisions of the past 30 years. The midwestern lines, which have presented the only detailed plan of readjustment before us, based that plan on the so-called 28277 scale prescribed in *Official Western Trunk Line Divisions,* 269 I.C.C. 765.

The midwestern plan impresses us as complicated and artificial in respect of the proposal to establish breaking points on or near the eastern border of transcontinental territory, where in some cases no actual interchange takes place. Nor do we agree that primary intermediate divisions should be subject to a 15-percent minimum, as proposed.

The complainants in their requested findings do not specify any plan which could be relied on to give them substantially the amount of increased revenue which they seek. One of their witnesses suggested that the 28277 scale would be satisfactory for this purpose or alternatively an adaptation of the so-called 29886 scale, prescribed in *Official Southwestern Divisions,* 287 I.C.C. 553. The complainants favor scales in principle.

The defendants are opposed to the use of divisional scales for a number of reasons. They say that "the present group basis of publishing transcontinental divisions is highly de-

[fol. 873] sirable in light of the competitive conditions affecting the routing of transcontinental traffic." Here we agree in general with the defendants.

The fact that nearly all the major transcontinental railroads have important operations east of mountain-Pacific territory over either their own rails or those of subsidiary companies is a complication of a kind not involved except to a minor extent in the interterritorial divisions cases of the past in which divisional scales were prescribed and found to be generally acceptable. The transcontinental class and commodity rates, applying over maximum distances, are broadly grouped in both the East and West. We see no practical reason for divisions reflecting 50-mile blocks, which might indeed prove to be inconsistent with the rate structure. We therefore prescribe specific divisions between representative points set forth in Appendix B.

Grouping—We deem it desirable to continue the common basis of divisions to and from Seattle, Portland, San Francisco, and Los Angeles and interior points in reasonable proximity to those cities. Different bases should apply, however, for the rapidly growing intermountain cities—Reno, Las Vegas, Phoenix, Spokane, and Boise.

The existing eastern groups appear to be suitable for use in dividing rates to and from the 4 Pacific port cities, except that there seems to be no good reason for continuing the small Bessemer, Pa., group separately from Pittsburgh. Since these groups are not used in connection with the new class rates to and from Phoenix, we are of the view that they may properly be discarded in dividing the Phoenix rates. It is believed that there should be a specific delineation of a group of Illinois stations on eastern and southern lines, including also Evansville, Vincennes, and Terre Haute, Ind. (South-Eastern Illinois, as more specifically described in Appendix B).

The present divisional groups in midwestern territory appear to be less well defined. The points in that territory used in Appendix B, therefore, are intended to be in the

nature of key points as a guide to the establishment of such groups as the interested railroads may agree upon.

Interchange Points—Differences of opinion concerning interchange or dividing points are slight. Since the great majority of the traffic to and from the East moves through Chicago, Peoria, or St. Louis, it is generally agreed that those cities should be the principal dividing points, and we have been governed accordingly. In addition, we have provided for the use of Mackinaw City, Mich., and for Kewaunee, Wis., the latter being representative for cross-lake routes. Potomac Yard, Va., and Cincinnati, Ohio, are used as representative dividing points on movements through southern territory.

There are numerous interchange points in Illinois of minor importance which may properly be given the same divisional bases as one of the other major dividing points. East Joliet and perhaps also Kankakee, Dwight, and Streator might well be on the Chicago basis. A Peoria divisional group could also appropriately embrace Bloomington, Decatur, and Springfield. Illinois points south of East St. Louis—Flinton, Thebes, and Cairo—should be on the St. Louis basis.

We do not agree with the proposal of the complainants that Kansas City and Omaha should be primary dividing points when traffic is interchanged there with the Wabash. Nor do we consider it necessary or desirable that East [fol. 874] Hannibal, Ill., continue to be a dividing point. In our opinion the Wabash should be treated as a western carrier when it performs service west of St. Louis or Springfield.

A minor complication occurs when traffic moves through two or more primary dividing points. On shipments through Chicago or Peoria and St. Louis, the latter should be the principal dividing point. We agree with the midwestern lines that, when traffic moves through Peoria and Chicago, Peoria should be the dividing point. This disposition would be inconsistent with the contention of the Missouri-Illinois

that Flinton should be the primary dividing point on traffic which passes through both Flinton and St. Louis. On such traffic we believe that St. Louis should be the primary point.

Between the midwestern and the transcontinental lines we have provided for interchanges at Duluth, the Twin Cities, Omaha, Kansas City, El Paso, Denver, and Pueblo. As representative of minor southwestern points of interchange with the AT&SF we have used Floydada, Tex., Aberdeen, S. Dak., and Oakes, N. Dak., have similarly been used for midwest-northwest territory.

Traffic which is interchanged between eastern and western railroads at St. Louis or East St. Louis generally requires the service of an intermediate terminal rail or motor carrier for the river crossing. At present the cost of that service on transcontinental traffic is borne by the western lines on both eastbound and westbound shipments. The same arrangement formerly prevailed on all interterritorial traffic at St. Louis but as a result of the decisions of the Commission relating to divisions of rates between official territory, on the one hand, and southwestern and western trunk-line territories, on the other hand, the eastern lines pay intermediate charges on westbound shipments to those territories and the western lines pay them on eastbound freight. It is generally agreed by the parties that this arrangement should be extended to transcontinental shipments.

Transit and Reconsignment—The midwestern lines ask that certain traffic subject to transit arrangements and reconsignment, involving unusual out-of-line or back-haul service, be excepted from application of the divisions prescribed in this report. There are now special divisions for this traffic which have resulted from agreements between midwestern and transcontinental lines. It is stated that, although some of the traffic moves to or from eastern territory, the proportions of the eastern railroads are not affected by these special divisions.

As an illustration of this traffic, the midwestern lines cite a transit movement of barley from the Twin Cities to Chicago and malt from that point through Council Bluffs to the Pacific coast. They assert that any general basis of divisions would be inappropriate for such traffic, and that any revision of the special divisions thereon "that might be called for in the light of the divisions prescribed on the general body of traffic could probably be worked out by negotiations between the interested carriers."

The exception proposed by the midwestern lines is opposed by both the transcontinental lines and the complainants. Whether the latter would be adversely affected by the [fol. 875] exception, as they fear, is not clear. On the whole, we are inclined to believe that the safest course would be not to require such exceptions from the prescribed divisions, thus laying upon the midwestern lines the burden of justifying their proposed exceptions either in intercarrier negotiations or upon further consideration by the Commission, as they suggest.

Findings

(1) We find that the present divisions of joint interterritorial rates between points in official territory and points in mountain-Pacific territory, as defined in the complaint in No. 31503, are unjust, unreasonable, and inequitable.

(2) We find that the present divisions of joint interterritorial rates between points in midwestern territory and points in transcontinental territory (including Montana), as defined in the complaint in No. 31503, Sub No. 1, are unjust, unreasonable and inequitable.

(3) We find that just, reasonable and equitable divisions of the joint rates referred to in findings (1) and (2) hereinabove would be those set forth in Appendix B.

Premises considered *it is the Order* of the Examiners that the complainants, cross-complainants, and defendants, according as they participate in the transportation, be, and

they are hereby, notified and required to establish within 90 days after the date on which this recommended report and order becomes the report and order of the Commission, and thereafter apply divisions of joint all-rail interstate rates on classes and commodities between points in official territory, on the one hand, and points in mountain-Pacific territory, on the other hand, and between points in mid-western territory, on the one hand, and points in transcontinental territory (including Montana), on the other hand, in the form of percentages as shown for the respective groups in Appendix B to this report.

It is the further Order of the Examiners that the said complainants, cross-complainants, and defendants, according as they participate in the transportation, be, and they are hereby, notified and required to cease and desist on and after 90 days from the date on which this recommended report and order becomes the report and order of the Commission, and thereafter to abstain from asking, demanding, collecting, or receiving divisions of said joint rates upon bases other than those herein prescribed.

And it is the further Order of the Examiners that this order shall continue in force until further order of the Commission.

By the Commission, Howard Hosmer and Oren G. Barber, Hearing Examiners.

Dated at Washington, D. C., this day of A. D. 1960.

Harold D. McCoy, Secretary.

(Seal)

[fol. 876] APPENDIX A

Notes

2. Individual carriers will sometimes be referred to by their initials or other abbreviations.

3. Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming.

4. The exceptions are as follows:—Wyoming—stations on and east of the line of the UP, Laramie and east; Colorado—stations on and east of the line of the C&S between Cheyenne, Wyo., and Trinidad, Colo.; New Mexico—stations on the line of the Texas-New Mexico Railway Company.

5. The term "transcontinental territory" as used in this complaint embraces all of Arizona, California, Oregon, and Washington, substantially all of Nevada, and the western portions of Idaho, Utah, and New Mexico. "Midwestern territory" includes all of western territory east of the Rocky Mountains except Montana, Wyoming, North Dakota, and northern Minnesota. Sub No. 1, however, covers divisions of interterritorial and intraterritorial joint rates to and from Montana points over routes via northern lines.

6. The oldest method of dividing joint rates disclosed by railroad history is the mileage prorate or some modification thereof. In 1893 a spokesman for the transcontinental lines in a controversy over divisions referred to the time-honored character of such a basis in the following words:

"The question which we are now called to consider has been brought up repeatedly within the last 20 years. It has been often discussed and as often settled on the present basis. * * * We contend that a basis of divisions which has stood the test of time

since the first overland roads were completed—now nearly a quarter of a century—must have been founded on correct principles; principles which govern divisions of revenue on through traffic not only throughout the United States, but the world over. I need not go outside this meeting to find ample proof of what I say, namely, that the principles which govern our present basis of divisions apply generally on through traffic."

7. *Dayton-Goose Creek Ry. Co.* v. *United States,* 263 U.S. 456, 478.

8. Before the hearings began it was suggested to the parties that a general investigation of the divisions on the Commission's initiative might be preferable to a trial solely on the issues raised by the complaints. In such an investigation the participation of the Commission's Cost Finding Section would perhaps have been possible and salutary. The complainants and the midwestern lines acquiesced in the suggestion, but the defendants did not. The suggestion was not pressed.

9. The distinction between way and through trains recognized in Rail Form A is based on the type of service performed by the two classes. Way trains are those which perform a large amount of station switching at intermediate points and assemble cars which may or may not be picked up subsequently by through trains. The latter are operated primarily for the [fol. 877] purpose of moving traffic between distribution points or terminals of designated operating divisions. Traffic in way trains is assigned unit costs reflecting the higher costs of that service. (The foregoing definitions are used by the Cost Finding Section in collecting periodic data for a 7-day study of loaded and empty car-miles and other statistics on a sample basis).

10. *Divisions of Freight Rates,* 203 I.C.C. 299, 323; *Class Rates, Mountain-Pacific Territory,* 296 I.C.C. 555, 609.

11. Table 4 indicates that the fully distributed costs in the eastern district and for the 10 mountain-Pacific railroads are at approximately the same level at the short hauls whether the costs are based on identical loads or territorial average loads. The line-haul costs of the 10 mountain-Pacific roads are lower than those in the eastern district, resulting in the indexes of costs for the 10 mountain-Pacific railroads being less as the hauls increase. The costs of the 7 interterritorial railroads are slightly less than those of the 10 mountain-Pacific railroads. The costs of the western trunkline and southwestern territories are somewhat below those of the 10 mountain-Pacific railroads and the 7 interterritorial railroads. The differences in costs between the 10 mountain-Pacific railroads and the 28300 territory railroads, excluding the 7 interterritorial railroads, are less than the differences between the eastern district and the Pocahontas region or the southern region. (p. 601)

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Summary.—Comparisons of territorial costs of the 10 mountain-Pacific railroads situated entirely within mountain-Pacific territory, the 7 interterritorial railroads, and the railroads within western trunkline and southwestern territories, excluding 7 interterritorial railroads, show less differences in costs than exist between the eastern district, Pocahontas region, and southern region where a single class rate scale is now in effect.

The more significant comparisons are at 300 short-line miles which is the approximate average haul of carload traffic moving within mountain-Pacific territory and at hauls between 500 and 1,000 short-line miles, which are the approximate range of hauls

within mountain-Pacific territory of the interterritorial traffic. At 300 miles the costs of the 10 mountain-Pacific railroads are about 2 to 10 percent higher than the level of costs for the United States as a whole. At 500 miles the costs of the same 10 mountain-Pacific railroads are from zero to 7 percent higher than the United States costs. At 1,000 miles the costs for the 10 mountain-Pacific railroads are from 3 percent below to 4 percent above those for the United States average. (p. 611)

12. *Southwestern-Official Divisions,* 234 I.C.C. 135, 147; *Official-Southwestern Divisions,* 287 I.C.C. 553, 564.

13. Sources of the figures showing passenger deficits for the eastern district, Pocahontas region, and western district are the Commission's Annual Reports on Transport Statistics in the United States for the years indicated.

The passenger deficits of the individual transcontinental lines in 1948, 1949, and 1959 were as follows: (thousands)

[fol. 878]

	1948	1949	1959
AT&SF	$ 23,269	$ 29,892	$ 36,562
D&RGW	4,955	5,295	5,109
GN	14,526	18,391	20,845
NP	11,719	12,143	16,735
SP	24,540	34,420	37,159
UP	28,463	39,191	42,779
	$107,472	$139,332	$159,189

(The source of the figures for 1948 and 1949 above shown is Monthly Comment on Transportation Statistics, Bureau of Transport Economics and Statistics, ICC, May 12, 1950, p. 3. The source for the figures for 1959 is the Commission's Annual Report on Transport Statistics for 1959.)

14. The total passenger deficits for all class I railroads in 1948-1959, shown in the Commission's Annual Report on Transport Statistics, were as follows: (thousands)

1948	$559,782
1949	649,627
1950	508,508
1951	680,822
1952	642,390
1953	704,538
1954	669,533
1955	636,693
1956	696,938
1957	723,483
1958	610,424
1959	543,804

15. These estimated savings do not take into account the Federal income tax on the enhanced earnings. It may also be observed here, that the defendants' estimated losses for reductions in revenue due to various proposals for revision of their divisions similarly do not take into account the Federal income tax.

16. Sources of the figures showing net railway operating income from freight service for the eastern district, Pocahontas region, and western district are the Commission's Annual Reports on Transport Statistics in the United States for the years indicated.

The freight net railway operating income of the individual transcontinental lines in 1948, 1949, and 1959 was as follows: (thousands)

	1948	1949	1959
AT&SF	$ 91,985	$ 85,541	$ 96,119
D&RGW	17,111	13,618	16,305
GN	41,726	38,936	45,056
NP	31,859	26,161	31,303
SP	60,136	62,431	83,277
UP	71,122	61,475	80,181
	$313,939	$288,162	$352,241

[fol. 879]

17. Passenger deficits and freight net railway operating income of individual midwestern lines in 1948, 1949, and 1959 are shown below.

Passenger deficits (000)

	1948	1949	1959
CB&Q	$ 14,258	$ 20,174	$ 21,627
C&NW	17,617	22,319	13,476
CMStP&P	20,574	24,975	20,145
CRI&P	8,045	11,009	18,214
IC	9,065	12,982	15,464
MKT	5,588	5,984	3,417
GM&O	5,233	5,587	3,425
MoPac	12,059	11,774	16,561
StLSF	8,488	9,205	7,726
	$100,927	$124,009	$120,055

Freight Net Railway Operating Income (000)

	1948	1949	1959
CB&Q	$ 46,973	$ 39,789	$ 41,059
C&NW	27,627	25,102	16,600
CMStP&P	36,088	35,914	33,796
CRI&P	29,937	30,844	30,058
IC	38,835	38,167	34,253
MKT	14,913	13,668	7,198
GM&O	14,330	12,596	8,968
MoPac	38,634	27,975	49,760
StLSF	19,878	19,421	19,355
	$267,215	$243,476	$241,047

(The source of the figures for 1948 and 1949 above shown is Monthly Comment on Transportation Statistics, Bureau of Transport Economics and Statistics, I.C.C., May 12, 1950, p. 3. The source of the figures for 1959 is the Commission's Annual Report on Transport Statistics for 1959.)

18. *United States* v. *Abilene & S. Ry. Co.*, 265 U.S. 274, 285.

APPENDIX B

Prescribed Divisions

Railroad groups are referred to by the following designations: E, Eastern; S, Southern; W, Western; MW, Midwestern; TC, Transcontinental.

The Seaboard-New England group of points referred to in Section I is also known as groups A and B. The Syracuse group referred to in Section II is also known as the trunk-line interior group or group C. The Pittsburgh group referred to in Section III is also known as group E. The Detroit group referred to in Section IV is also known as Group F. South-Eastern Illinois referred to in Section V includes points on southern or eastern railroads in Illinois south and east of the line of the Atchison, Topeka & Santa Fe between Chicago and Peoria and the line of the Gulf Mobile & Ohio between Peoria and East St. Louis, and also Evansville, Vincennes, and Terre Haute, Ind.

SECTION I

Between-	Interchange Points	Percentages E	MW	TC
1. Seaboard - New England Group and Seattle, Portland, Los Angeles, San Francisco	Chicago	32		68
	do. -Kansas City or Council Bluffs	32	13	55
	do. Denver	32	27	41
	Peoria	34		66
	do. Kansas City or Council Bluffs	34	12	54
	do. Denver or Pueblo	34	24	42
	St. Louis	35		65
	do. Kansas City	35	10	55
	do. Denver or Pueblo	35	23	42
2. Seaboard - New England Group and Seattle, Portland	Chicago - Twin Cities	32	13	55
	Peoria - do.	34	14	52
	St. Louis - do.	35	15	50
	Mackinaw City - Duluth	32	13	55
	Kewaunee- Twin Cities	32	12	56
	do. Council Bluffs	32	15	53
3. Seaboard - New England Group and Los Angeles, San Francisco	Chicago - El Paso	32	34	34
	Peoria - do.	34	33	33
	St. Louis - do.	35	31	34
	do. Floydada	35	22	43

[fol. 880]

Between-	Interchange Points	Percentages E	MW	TC
4. Seaboard - New England Group and Reno, Las Vegas, Boise, Spokane	Chicago	36		64
	do. - Kansas City or Council Bluffs	36	16	48
	do. - Denver	36	29	35
	Peoria -	37		63
	do. Kansas City or Council Bluffs	37	13	50
	do. Denver	37	27	36
	St. Louis	38		62
	do. Kansas City	38	13	49
	do. Denver, Pueblo	38	25	37
5. Seaboard - New England Group and Spokane	Chicago - Twin Cities	36	14	50
	Peoria - do.	37	15	48
	St. Louis - do.	38	17	45
	Mackinaw City - Duluth	36	15	49
	Kewaunee - Twin Cities	36	13	51
	do. - Council Bluffs	36	14	50

		E	S	W
6. Seaboard - New England Group and Los Angeles, San Francisco	Potomac Yard - New Orleans	15	28	57
	Cincinnati - New Orleans	23	20	57

		E	S	MW	TC
7. Seaboard - New England Group and Los Angeles, San Francisco	Potomac Yard - Memphis El Paso	15	23	28	34
	Cincinnati - Memphis El Paso	24	12	27	37

		E	MW	TC
8. Boston and Phoenix	Chicago	36		64
	do. - El Paso	36	41	23
	do. - Kansas City or Council Bluffs	36	16	48
	Peoria -	40		60
	do. - El Paso	40	38	22
	do. - Kansas City or Council Bluffs	40	13	47
	St. Louis	42		58
	do. - El Paso	42	37	21
	do. - Kansas City	42	12	46
	do. - Floydada	42	18	40

		E	S	W
9. Boston and Phoenix	Potomac Yard - New Orleans	19	31	50
	Cincinnati - New Orleans	28	23	49

[fol. 881]

SECTION I

	Between-	Interchange Points	Percentages E	S	MW	TC
10.	Boston and Phoenix	Cincinnati - Memphis - El Paso	32	14	31	23
		Potomac Yard - Memphis - El Paso	19	26	32	23

			E		MW	TC
11.	New York and Phoenix	Chicago	34			66
		do. - El Paso	34		39	27
		do. - Kansas City or Council Bluffs	34		16	50
		Peoria -	38			62
		do. - El Paso	38		38	24
		do. - Kansas City or Council Bluffs	38		13	49
		St. Louis	39			61
		do. - El Paso	39		37	24
		do. - Kansas City	39		11	50
		do. - Floydada	39		25	36
		Potomac Yard - New Orleans	16	(S)	32	52
		Cincinnati - New Orleans	26	(S)	24	50

			E	S	MW	TC
		Cincinnati - Memphis - El Paso	29	15	32	24
		Potomac Yard - Memphis El Paso	15	27	33	25

			E		MW	TC
12.	Philadelphia and Phoenix	Chicago	33			67
		do.- Kansas City or Council Bluffs.	33		17	50
		do.- El Paso	33		42	25
		Peoria -	37			63
		do. - Kansas City or Council Bluffs	37		13	50
		do. - El Paso	37		39	24
		St. Louis	38			62
		do. - Kansas City	38		12	50
		do. - El Paso	38		38	24
		do. - Floydada	38		25	37

		E	S	W
	Potomac Yard - New Orleans	15	32	53
	Cincinnati - New Orleans	24	24	52

		E	S	MW	TC
	Cincinnati - Memphis - El Paso	26	16	33	25
	Potomac Yard - Memphis - El Paso	15	27	33	25

			E	W
13.	Boston and Albuquerque, N. Mex.	Chicago	45	55
		Peoria	48	52
		St. Louis	51	49

[fol. 882]

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SECTION 1

		Interchange Points	Percentages E	W
14.	Between- Boston and Carlsbad, N. Mex.	Chicago	45	55
		Peoria	49	51
		St. Louis	52	48
15.	Boston and Tucumcari, N. Mex.	Chicago	48	52
		Peoria	53	47
		St. Louis	56	44
16.	New York and Albuquerque	Chicago	42	58
		Peoria	46	54
		St. Louis	48	52
17.	New York and Carlsbad	Chicago	43	57
		Peoria	47	53
		St. Louis	49	51
18.	New York and Tucumcari	Chicago	46	54
		Peoria	51	49
		St. Louis	53	47
19.	Philadelphia and Albuquerque	Chicago	41	59
		Peoria	45	55
		St. Louis	47	53
20.	Philadelphia and Carlsbad	Chicago	42	58
		Peoria	46	54
		St. Louis	48	52
21.	Philadelphia and Tucumcari	Chicago	45	55
		Peoria	50	50
		St. Louis	52	48
22.	Boston and Salt Lake City, Utah	Chicago	40	60
		Peoria	41	59
		St. Louis	43	57
23.	Boston and Pocatello, Idaho	Chicago	36	64
		Peoria	39	61
		St. Louis	41	59

[fol. 883]

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	Between-	Interchange Points	Percentages E	W
24.	Boston and Rock Springs, Wyo.	Chicago	41	59
		Peoria	44	56
		St. Louis	45	55
25.	Boston and Grand Junction, Colo.	Chicago	40	60
		Peoria	43	57
		St. Louis	46	54
26.	New York and Salt Lake City	Chicago	37	63
		Peoria	39	61
		St. Louis	41	59
27.	New York and Pocatello	Chicago	34	66
		Peoria	37	63
		St. Louis	39	61
28.	New York and Rock Springs	Chicago	39	61
		Peoria	42	58
		St. Louis	43	57
29.	New York and Grand Junction	Chicago	38	62
		Peoria	42	58
		St. Louis	43	57
30.	Philadelphia and Salt Lake City	Chicago	35	65
		Peoria	37	63
		St. Louis	39	61
31.	Philadelphia and Pocatello	Chicago	33	67
		Peoria	36	64
		St. Louis	38	62
32.	Philadelphia and Rock Springs	Chicago	38	62
		Peoria	41	59
		St. Louis	42	58
33.	Philadelphia and Grand Junction	Chicago	37	63
		Peoria	41	59
		St. Louis	42	58

[fol. 884]

SECTION I

		Interchange Points	Percentages E	MW	TC
34.	Between- Boston and Billings, Mont.	Chicago	43		57
		Chicago -Twin Cities	43	16	41
		Peoria	45		55
		Peoria -Twin Cities	45	16	39
		St. Louis	46		54
		Kewaunee - Twin Cities	45	15	40
		Mackinaw City - Duluth	41	17	42
35.	Boston and Great Falls, Mont.	Chicago	40		60
		Chicago -Twin Cities	40	15	45
		Peoria	43		57
		do. -Twin Cities	43	14	43
		St. Louis	42		58
		Kewaunee - Twin Cities	41	14	45
		Mackinaw City - Duluth	41	17	42
36.	Boston and Butte, Mont.	Chicago	40		60
		do. -Twin Cities	40	15	45
		Peoria	41		59
		do. -Twin Cities	41	14	45
		St. Louis	42		58
		Kewaunee -Twin Cities	41	13	46
		Mackinaw City - Duluth	38	16	46
37.	New York, Philadelphia and Billings	Chicago	42		58
		do. -Twin Cities	42	17	41
		Peoria	42		58
		do. -Twin Cities	42	17	41
		St. Louis	43		57
		Kewaunee - Twin Cities	43	15	42
		Mackinaw City - Duluth	40	18	42
38.	New York, Philadelphia and Butte	Chicago	37		63
		do. -Twin Cities	37	15	48
		Peoria	38		62
		do. -Twin Cities	38	15	47
		St. Louis	39		61
		Kewaunee -Twin Cities	39	14	47
		Mackinaw City - Duluth	37	16	47
39.	New York, Philadelphia and Great Falls	Chicago	38		62
		do. -Twin Cities	38	16	46
		Peoria	39		61
		do. -Twin Cities	39	15	46
		St. Louis	40		60
		Kewaunee -Twin Cities	40	14	46
		Mackinaw City - Duluth	40	17	43

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SECTION II

Between -	Interchange Points	Percentages E	MW	TC
1. Syracuse Group and Seattle, Portland, Los Angeles, San Francisco	Chicago	27		73
	do. -Kansas City or Council Bluffs	27	14	59
	do. -Denver	27	27	46
	Peoria	30		70
	do. -Kansas City or Council Bluffs	30	10	60
	St. Louis	30		70
	do. -Kansas City	30	10	60
	do. -Denver or Pueblo	30	23	47
2. Syracuse Group and Seattle, Portland	Chicago - Twin Cities	26	13	61
	Peoria - do.	29	14	57
	St. Louis - do.	29	15	56
	Mackinaw City - Duluth	27	14	59
	Kewaunee - Twin Cities	27	12	61
	do. - Council Bluffs	27	14	59
3. Syracuse Group and Los Angeles, San Francisco	Chicago - El Paso	27	34	39
	Peoria - do.	30	32	38
	St. Louis - do.	30	31	39
	do. -Floydada, Texas	30	22	48
		E	S	W
	Potomac Yard - New Orleans	15	28	57
	Cincinnati - New Orleans	19	20	61
		E	S	MW TC
	Cincinnati - Memphis-El Paso	21	12	27 40
4. Syracuse Group and Las Vegas, Reno, Boise and Spokane		E		MW TC
	Chicago	29		71
	do. - Kansas City or Council Bluffs	29	17	54
	do. - Denver	29	30	41
	Peoria	31		69
	do. - Kansas City or Council Bluffs	31	13	56
	do. - Denver	31	28	41
	St. Louis	32		68
	do. - Kansas City	32	13	55
	do. - Denver or Pueblo	32	24	44

[fol. 886]

Between —	Interchange Points	Percentages E	MW	TC
5. Syracuse Group and Spokane	Chicago - Twin Cities	29	15	56
	Peoria - do.	31	14	55
	St. Louis - do.	32	18	50
	Mackinaw City - Duluth	29	15	56
	Kewaunee - Twin Cities	29	14	57
	do. - Council Bluffs	29	15	56
6. Syracuse and Phoenix	Chicago	29		71
	do. - Kansas City or Council Bluffs	29	17	54
	do. - El Paso	29	45	26
	Peoria	34		66
	do. - Kansas City or Council Bluffs	34	13	53
	do. - El Paso	34	41	25
	St. Louis	35		65
	do. - Kansas City	35	12	53
	do. - El Paso	35	39	26
	do. - Floydada	35	26	39

	E	S	W
Potomac Yard - New Orleans	17	31	52
Cincinnati - New Orleans	23	26	51

	E	S	MW	TC
Cincinnati - Memphis El Paso	25	15	33	27

		E	W
7. Syracuse and Salt Lake City	Chicago	32	68
	Peoria	36	64
	St. Louis	37	63
8. Syracuse and Pocatello	Chicago	28	72
	Peoria	33	67
	St. Louis	34	66
9. Syracuse and Rock Springs	Chicago	33	67
	Peoria	37	63
	St. Louis	38	62
10. Syracuse and Grand Junction	Chicago	32	68
	Peoria	37	63
	St. Louis	39	61
11. Syracuse and Albuquerque	Chicago	38	62
	Peoria	42	58
	St. Louis	45	55

[fol. 887]

SECTION II

	Between -	Interchange Points	Percentages E	W	TC
12.	Syracuse and Carlsbad	Chicago	40		60
		Peoria	43		57
		St. Louis	45		55
13.	Syracuse and Tucumcari	Chicago	41		59
		Peoria	47		53
		St. Louis	49		51
14.	Syracuse and Billings		E	MW	TC
		Chicago	35		65
		do. -Twin Cities	35	18	47
		Peoria	39		61
		do. -Twin Cities	39	17	44
		St. Louis	40		60
		Kewaunee -Twin Cities	36	20	44
		Mackinaw City- Duluth	34	19	47
15.	Syracuse and Butte	Chicago	32		68
		do. -Twin Cities	32	16	52
		Peoria	35		65
		do. -Twin Cities	35	15	50
		St. Louis	35		65
		Kewaunee -Twin Cities	33	15	52
		Mackinaw City - Duluth	31	17	52
16.	Syracuse and Great Falls	Chicago	33		67
		do. -Twin Cities	33	17	50
		Peoria	36		64
		do. -Twin Cities	36	16	48
		St. Louis	36		64
		Kewaunee -Twin Cities	34	15	51
		Mackinaw City - Duluth	34	19	47

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SECTION III

Between -	Interchange Points	Percentages E	MW	TC
1. Pittsburgh Group and Seattle, Portland, San Francisco, Los Angeles	Chicago	20		80
	do. -Kansas City or Council Bluffs	20	15	65
	do. -Denver	20	29	51
	Peoria -	22		78
	do. -Kansas City or Council Bluffs	22	12	66
	do. -Denver	22	26	52
	St. Louis	23		77
	do. -Kansas City	23	11	66
	do. - Denver, Pueblo	23	25	52
2. Pittsburgh Group and Seattle, Portland	Chicago - Twin Cities	20	14	66
	Peoria - do.	22	15	63
	St. Louis do.	23	17	60
	Mackinaw City - Duluth	20	15	65
	Kewaunee - Twin Cities	20	13	67
	do. -Council Bluffs	20	18	62
3. Pittsburgh Group and Los Angeles, San Francisco	Chicago - El Paso	20	38	42
	Peoria - do.	22	35	43
	St. Louis - do.	23	34	43
	do. - Floydada	23	24	53

		E	S	MW	TC
	Cincinnati - New Orleans	15	22		63
	Cincinnati - Memphis El Paso	15	13	29	43

		E	MW	TC
Pittsburgh Group and Las Vegas, Reno, Boise and Spokane	Chicago	22		78
	do. -Kansas City or Council Bluffs	22	18	60
	do. -Denver	22	34	44
	Peoria -	25		75
	do. -Kansas City or Council Bluffs	25	15	60
	do. -Denver	25	31	44
	St. Louis	26		74
	do. -Kansas City or Council Bluffs	26	13	61
	do. -Denver, Pueblo	26	30	44
5. Pittsburgh Group and Spokane	Chicago -Twin Cities	22	17	61
	Peoria - do.	25	13	62
	St. Louis - do.	26	20	54
	Mackinaw City - Duluth	22	18	60
	Kewaunee -Twin Cities	22	15	63

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Between-	Interchange Points	Percentage		
		E	MW	TC
6. Buffalo and Phoenix	Chicago	25		75
	do. -Kansas City or Council Bluffs	25	19	56
	do. -El Paso	25	49	26
	Peoria	30		70
	do. -Kansas City or Council Bluffs	30	14	56
	do. -El Paso	30	44	26
	St. Louis	33		67
	do. -Kansas City	33	13	54
	do. -El Paso	33	41	26
	do. -Floydada	33	30	37

	E	S	W
Cincinnati - New Orleans	20	27	53

	E	S	MW	TC
Cincinnati - Memphis - El Paso	22	16	36	26

		E	MW	TC
7. Pittsburgh and Phoenix	Chicago	25		75
	do. -Kansas City or Council Bluffs	25	19	56
	do. -El Paso	25	49	26
	Peoria	29		71
	do. -Kansas City or Council Bluffs	29	14	57
	do. -El Paso	29	44	27
	St. Louis	31		69
	do. -Kansas City	31	13	56
	do. -El Paso	31	42	27
	do. -Floydada	31	28	41

	E	S	W
Cincinnati - New Orleans	16	28	56

	E	S	MW	TC
Cincinnati - Memphis - El Paso	18	17	37	28

		E	MW	TC
8. Cleveland and Phoenix	Chicago	19		81
	do. -Kansas City or Council Bluffs	19	19	62
	do. -El Paso	19	50	31
	Peoria -	25		75
	do. -Kansas City or Council Bluffs	25	15	60
	do. -El Paso	25	45	30
	St. Louis	28		72
	do. -Kansas City	28	13	59
	do. -El Paso	28	43	29
	do. -Floydada	28	29	43

	E	S	W
Cincinnati - New Orleans	15	28	57

	E	S	MW	TC
Cincinnati - Memphis - El Paso	16	16	37	31

SECTION III

	Between -	Interchange Points	Percentages E	Percentages W
9.	Buffalo and Albuquerque	Chicago	32	68
		Peoria	38	62
		St. Louis	40	60
10.	Buffalo and Carlsbad	Chicago	33	67
		Peoria	39	61
		St. Louis	41	59
11.	Buffalo and Tucumcari	Chicago	35	65
		Peoria	38	62
		St. Louis	40	60
12.	Pittsburgh and Albuquerque	Chicago	32	68
		Peoria	37	63
		St. Louis	38	62
13.	Pittsburgh and Carlsbad	Chicago	33	67
		Peoria	38	62
		St. Louis	39	61
14.	Pittsburgh and Tucumcari	Chicago	35	65
		Peoria	40	60
		St. Louis	42	58
15.	Cleveland and Albuquerque	Chicago	27	73
		Peoria	32	68
		St. Louis	36	64
16.	Cleveland and Carlsbad	Chicago	28	72
		Peoria	33	67
		St. Louis	37	63
17.	Cleveland and Tucumcari	Chicago	30	70
		Peoria	37	63
		St. Louis	41	59
18.	Buffalo and Salt Lake City	Chicago	28	72
		Peoria	33	67
		St. Louis	35	65
19.	Buffalo and Pocatello	Chicago	25	75
		Peoria	29	61
		St. Louis	33	67
20.	Buffalo and Rock Springs	Chicago	29	71
		Peoria	33	67
		St. Louis	35	65

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SECTION III

	Between -	Interchange Points	Percentages E	W
21.	Buffalo and Grand Junction	Chicago	28	72
		Peoria	32	68
		St. Louis	37	63
22.	Pittsburgh and Salt Lake City	Chicago	27	73
		Peoria	30	70
		St. Louis	31	69
23.	Pittsburgh and Pocatello	Chicago	24	76
		Peoria	28	72
		St. Louis	31	69
24.	Pittsburgh and Rock Springs	Chicago	29	71
		Peoria	33	67
		St. Louis	34	66
25.	Pittsburgh and Grand Junction	Chicago	28	72
		Peoria	32	68
		St. Louis	34	66
26.	Cleveland and Salt Lake City	Chicago	23	77
		Peoria	26	74
		St. Louis	29	71
27.	Cleveland and Pocatello	Chicago	21	79
		Peoria	24	76
		St. Louis	28	72
28.	Cleveland and Rock Springs	Chicago	24	76
		Peoria	29	71
		St. Louis	31	69
29.	Cleveland and Grand Junction	Chicago	25	75
		Peoria	28	72
		St. Louis	32	68

			E	MW	TC
30.	Pittsburgh and Billings	Chicago	31		69
		do. -Twin Cities	31	19	50
		Peoria	34		66
		do. -Twin Cities	34	19	47
		St. Louis	35		65
		Kewaunee - Twin Cities	35	19	46
		Mackinaw City - Duluth	33	19	48

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	Between-	Interchange Points	Percentages E	MW	TC
31.	Pittsburgh and Butte	Chicago	28		72
		do. -Twin Cities	28	17	55
		Peoria	30		70
		do. -Twin Cities	30	16	54
		St. Louis	32		68
		Kewaunee -Twin Cities	32	15	53
		Mackinaw City - Duluth	30	17	53
32.	Pittsburgh and Great Falls	Chicago	29		71
		do. -Twin Cities	29	18	53
		Peoria	31		69
		do. -Twin Cities	31	17	52
		St. Louis	31		69
		Kewaunee - Twin Cities	33	16	51
		Mackinaw City - Duluth	33	19	48
33.	Buffalo and Billings	Chicago	31		69
		do. -Twin Cities	31	19	50
		Peoria	35		65
		do. -Twin Cities	35	18	47
		St. Louis	37		63
34.	Buffalo and Butte	Chicago	28		72
		do. -Twin Cities	28	17	55
		Peoria	33		67
		do. -Twin Cities	33	16	51
		St. Louis	34		66
35.	Buffalo and Great Falls	Chicago	29		71
		do. -Twin Cities	29	18	53
		Peoria	32		68
		do. -Twin Cities	32	17	51
		St. Louis	33		67
36.	Cleveland and Billings	Chicago	27		73
		do. -Twin Cities	27	21	52
		Peoria	29		71
		do. -Twin Cities	29	20	51
		St. Louis	32		68
37.	Cleveland and Butte	Chicago	24		76
		do. -Twin Cities	24	18	58
		Peoria	26		74
		do. -Twin Cities	26	17	57
		St. Louis	28		72
38.	Cleveland and Great Falls	Chicago	25		75
		do. -Twin Cities	25	17	58
		Peoria	27		73
		do. -Twin Cities	27	18	55
		St. Louis	29		71

Between	Interchange Points	Percentages E	MW	TC
1. Detroit-Indianapolis Group and Seattle, Portland, San Francisco, Los Angeles	Chicago	16		84
	do. -Kansas City or Council Bluffs	16	16	68
	do. -Denver	16	31	53
	Peoria	17		83
	do. -Kansas City or Council Bluffs	17	13	70
	do. -Denver, Pueblo	17	28	55
	St. Louis	18		82
	do. -Kansas City	18	12	70
	-Denver, Pueblo	18	27	55
2. Detroit-Indianapolis Group and Seattle, Portland	Chicago - Twin Cities	16	15	69
	Peoria - do.	17	16	67
	St. Louis - do.	18	18	64
	Mackinaw City - Duluth	16	16	68
	Kewaunee - Twin Cities	16	14	70
	do. -Council Bluffs	16	19	65
3. Detroit-Indianapolis Group and San Francisco, Los Angeles	Chicago - El Paso	16	39	45
	Peoria - do.	17	37	46
	St. Louis - do.	18	36	46
	do. - Floydada	18	26	56
	Cincinnati - New Orleans	E 15	S 23	W 62
	Cincinnati - Memphis - El Paso	E 15	S 13	MW TC 30 42
4. Detroit-Indianapolis Group and Reno, Las Vegas, Spokane, and Boise	Chicago	E 17	MW	TC 83
	do. -Kansas City or Council Bluffs	17	16	67
	do. -Denver	17	35	48
	Peoria	19		81
	do. -Kansas City or Council Bluffs	19	15	66
	do. -Denver	19	32	49
	St. Louis	20		80
	do. - Kansas City	20	13	67
	do. - Denver	20	31	49
5. Detroit-Indianapolis Group and Spokane	Chicago - Twin Cities	17	16	67
	Peoria - do.	19	17	64
	St. Louis - do.	20	20	60
	Mackinaw City - Duluth	17	19	64
	Kewaunee - Twin Cities	17	17	66
6. Detroit and Phoenix	Chicago	19		81
	do. -Kansas City or Council Bluffs	19	20	61
	do. - El Paso	19	51	30
	Peoria	23		77
	do. -Kansas City or Council Bluffs	23	15	62
	do. -El Paso	23	47	30
	St. Louis	28		72
	do. -Kansas City	28	13	59
	do. El Paso	28	43	29
	do. Floydada	28	29	43
	Cincinnati -New Orleans	16	28	56
	Cincinnati - Memphis El Paso	E 18	S 16	MW TC 36 28

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Between-	Interchange Point	Percentages E	W	TC
7. Cincinnati and Phoenix	Chicago	19		81
	do.--Kansas City or Council Bluffs	19	19	62
	do.--El Paso	19	46	35
	Peoria	22		78
	do.--Kansas City or Council Bluffs	22	15	63
	do.--El Paso	22	48	30
	St. Louis	23		77
	do.--Kansas City	23	14	63
	do.--El Paso	23	46	31
	do.--Floydada	23	31	46
		E		
8. Detroit and Albuquerque	Chicago	26		74
	Peoria	31		69
	St. Louis	35		65
9. Detroit and Carlsbad	Chicago	26		74
	Peoria	31		69
	St. Louis	35		65
10. Detroit and Tucumcari	Chicago	29		71
	Peoria	35		65
	St. Louis	39		61
11. Cincinnati and Albuquerque	Chicago	26		74
	Peoria	29		71
	St. Louis	30		70
12. Cincinnati and Carlsbad	Chicago	26		74
	Peoria	30		70
	St. Louis	30		70
13. Cincinnati and Tucumcari	Chicago	29		71
	Peoria	33		67
	St. Louis	34		66
14. Detroit and Salt Lake City	Chicago	22		78
	Peoria	25		75
	St. Louis	28		72
15. Detroit and Pocatello	Chicago	19		81
	Peoria	22		78
	St. Louis	25		75
16. Detroit and Rock Springs	Chicago	23		77
	Peoria	27		73
	St. Louis	29		71
17. Detroit and Grand Junction	Chicago	23		77
	Peoria	24		76
	St. Louis	30		70
18. Cincinnati and Salt Lake City	Chicago	22		78
	Peoria	24		76
	St. Louis	24		76
19. Cincinnati and Pocatello	Chicago	19		81
	Peoria	21		79
	St. Louis	22		78
20. Cincinnati and Rock Springs	Chicago	23		77
	Peoria	25		75
	St. Louis	25		75

SECTION IV

Between -	Interchange Points	Percentages E		W
21. Cincinnati and Grand Junction	Chicago	23		77
	Peoria	24		76
	St. Louis	27		73
		E	MW	TC
22. Detroit and Billings	Chicago	25		75
	do. -Twin Cities	25	21	54
	Peoria	28		72
	do. -Twin Cities	28	21	51
	St. Louis	31		69
	Kewaunee - Twin Cities	26	20	54
	Mackinaw City - Duluth	24	22	54
23. Detroit and Butte	Chicago	22		78
	do. -Twin Cities	22	18	60
	Peoria	24		76
	do. -Twin Cities	24	18	58
	St. Louis	27		73
	Kewaunee - Twin Cities	23	17	60
	Mackinaw City - Duluth	21	19	60
24. Detroit and Great Falls	Chicago	23		77
	do. -Twin Cities	23	19	58
	Peoria	25		75
	do. -Twin Cities	25	19	56
	St. Louis	27		73
	Kewaunee - Twin Cities	24	18	58
	Mackinaw City - Duluth	24	22	54
25. Cincinnati and Billings	Chicago	25		75
	do. -Twin Cities	25	21	54
	Peoria	26		74
	do. -Twin Cities	26	21	53
	St. Louis	26		74
	Kewaunee - Twin Cities	32	18	50
	Mackinaw City - Duluth	31	20	49
26. Cincinnati and Butte	Chicago	22		78
	do. -Twin Cities	22	18	60
	Peoria	23		77
	do. -Twin Cities	23	18	59
	St. Louis			
	Kewaunee - Twin Cities	29	16	55
	Mackinaw City - Duluth	28	17	55
27. Cincinnati and Great Falls	Chicago	23		77
	do. - Twin Cities	23	19	58
	Peoria	24		76
	do. -Twin Cities	24	19	57
	St. Louis	23		77
	do. -Twin Cities	23	23	54
	Kewaunee - Twin Cities	30	16	54
	Mackinaw City - Duluth	32	19	49

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SECTION V

	Between-	Interchange Points	Percentages E	MW	TC
1.	South-Eastern Illinois and Seattle, Portland, San Francisco, Los Angeles	Chicago, Peoria, or St. Louis	15		85
		Chicago - Council Bluffs or Kansas City	15	16	69
		Chicago - Denver or Pueblo	15	30	55
		Peoria or St. Louis-Council Bluffs or Kansas City	15	12	73
		Peoria - Denver or Pueblo	15	28	57
		St. Louis - Denver or Pueblo	15	27	58
2.	South-Eastern Illinois and Seattle, Portland	Chicago - Twin Cities	15	14	71
		Peoria - do.	15	14	71
		St. Louis - do.	15	18	67
3.	South-Eastern Illinois and San Francisco, Los Angeles	Chicago - El Paso	15	39	46
		Peoria - El Paso	15	38	47
		St. Louis - El Paso	15	34	51
		St. Louis - Eloydada	15	26	59
4.	South-Eastern Illinois and Spokane, Reno, Las Vegas	Chicago, Peoria, or St. Louis	15		85
		Chicago - Council Bluffs or Kansas City	15	20	65
		Peoria or St. Louis-Council Bluffs or Kansas City	15	15	70
		Chicago - Denver or Pueblo	15	32	53
		Peoria - Denver or Pueblo	15	31	54
		St. Louis - Denver or Pueblo	15	30	55
5.	South-Eastern Illinois and Spokane	Chicago - Twin Cities	15	16	69
		Peoria - do.	15	17	68
		St. Louis - do.	15	19	66
6.	South-Eastern Illinois and Phoenix	Chicago, Peoria, or St. Louis	17		83
		Chicago - Kansas City	17	19	64
		Peoria - Kansas City	17	16	67
		St. Louis - Kansas City	17	15	68
		Chicago - El Paso	17	51	32
		Peoria - El Paso	17	49	34
		St. Louis - El Paso	17	49	34
		St. Louis - Floydada	17	33	50

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	Between-	Interchange Points	Percentages E	W	
7.	South-Eastern Illinois and Albuquerque	Chicago, Peoria, or St. Louis	23	77	
8.	South-Eastern Illinois and Carlsbad	Chicago, Peoria, or St. Louis	24	76	
9.	South-Eastern Illinois and Tucumcari	Chicago, Peoria, or St. Louis	26	74	
10.	South-Eastern Illinois and Salt Lake City	Chicago, Peoria, or St. Louis	19	81	
11.	South-Eastern Illinois and Pocatello	Chicago, Peoria, or St. Louis	19	81	
12.	South-Eastern Illinois and Rock Springs	Chicago, Peoria or St. Louis	22	78	
13.	South-Eastern and Grand Junction	Chicago, Peoria, or St. Louis	22	78	
			E	MW	TC
14.	South-Eastern Illinois and Billings	Chicago, Peoria or St. Louis	21		79
		Chicago - Twin Cities	21	22	57
		Peoria - Twin Cities	21	22	57
		St. Louis - Twin Cities	21	26	53
15.	South-Eastern Illinois and Butte	Chicago, Peoria, or St. Louis	19		81
		Chicago - Twin Cities	19	19	62
		Peoria - Twin Cities	19	19	62
		St. Louis - Twin Cities	19	23	58
16.	South-Eastern Illinois and Great Falls	Chicago, Peoria, or St. Louis	19		81
		Chicago - Twin Cities	19	20	61
		Peoria - Twin Cities	19	20	61
		St. Louis - Twin Cities	19	23	58

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	Between-	Interchange Points	Percentages MW	TC
1.	Chicago, Milwaukee, Peoria Group and Portland, Seattle	Twin Cities	22	78
		Council Bluffs or Kansas City	22	78
		Denver or Pueblo	39	61
2.	Chicago, Milwaukee Peoria Group and Spokane	Twin Cities	24	76
3.	Chicago, Milwaukee, Peoria Group and San Francisco, Los Angeles	Council Bluffs or Kansas City	22	78
		Denver or Pueblo	39	61
		El Paso	48	52
4.	Chicago, Milwaukee, Peoria Group and Reno, Las Vegas, Spokane	Council Bluffs or Kansas City	24	76
		Denver or Pueblo	42	58
5.	Chicago and Phoenix	El Paso	63	37
		Kansas City	27	73
		Denver	47	53
6.	Chicago and Boise	Council Bluffs or Kansas City	27	73
		Denver	46	54
7.	Chicago and Billings	Twin Cities	34	66
8.	Chicago and Butte	Twin Cities	28	72
9.	Chicago and Great Falls	Twin Cities	29	71
			MW	TC
10.	St. Louis, Davenport, Des Moines Group and Seattle, Portland, San Francisco, Los Angeles	Council Bluffs or Kansas City	17	83
		Denver or Pueblo	35	65
11.	St. Louis and Seattle, Portland	Twin Cities	25	75
12.	St. Louis, Davenport, Des Moines Group and San Francisco, Los Angeles	El Paso	45	55
		Floydada	33	67
13.	Des Moines Group and Seattle, Portland	Twin Cities	20	80
14.	St. Louis, Davenport, Des Moines Group and Reno, Las Vegas, Spokane	Council Bluffs or Kansas City	20	80
		Denver or Pueblo	40	60
15.	St. Louis and Spokane	Twin Cities	29	71
16.	Des Moines, Davenport and Spokane	Twin Cities	22	78

[fol. 899]

SECTION VI

	Between-	Interchange Points	Percentages MW	Percentages TC
17.	St. Louis and Boise	Kansas City	21	79
		Denver	43	57
18.	St. Louis and Phoenix	Kansas City	22	78
		Floydada	42	58
		El Paso	60	40
		Pueblo	44	56
19.	Des Moines and Phoenix	Kansas City	20	80
		Denver	37	63
		El Paso	58	42
		Floydada	42	58
20.	St. Louis and Billings	Twin Cities	38	62
21.	St. Louis and Butte	Twin Cities	32	68
22.	St. Louis and Great Falls	Twin Cities	33	67
23.	Des Moines and Billings	Twin Cities	30	70
24.	Des Moines and Butte	Twin Cities	25	75
25.	Des Moines and Great Falls	Twin Cities	26	74
26.	Twin Cities and San Francisco, Los Angeles	Council Bluffs	20	80
		Kansas City	23	77
		Denver	36	64
		El Paso	49	51
27.	Twin Cities and Reno, Las Vegas	Council Bluffs	22	78
		Denver	41	59
28.	Twin Cities and Phoenix	Kansas City	29	71
		El Paso	65	35
29.	Kansas City, Omaha and Seattle, Portland, San Francisco, Los Angeles	Denver or Pueblo	29	71

[Fol. 900]

SECTION IV

	Between-	Interchange Points	Percentages MW	TC
30.	Omaha and Seattle, Portland	Twin Cities	19	71
31.	Kansas City and Los Angeles, San Francisco	Twin Cities	23	77
32.	Kansas City and Los Angeles, San Francisco	El Paso Floydada	39 27	61 73
33.	Omaha and San Francisco, Los Angeles	El Paso	41	59
34.	Kansas City, Omaha and Reno, Las Vegas, Spokane	Denver or Pueblo	32	68
35.	Omaha and Spokane	Twin Cities	21	79
36.	Kansas	Twin Cities	26	74
37.	Omaha and Boise	Denver	34	66
38.	Kansas City and Boise	Denver	38	62
39.	Kansas City and Phoenix	Pueblo or Floydada El Paso	35 55	65 45
40.	Omaha and Phoenix	El Paso	58	42
41.	Kansas City and Billings	Twin Cities	36	64
42.	Kansas City and Butte	Twin Cities	31	69
43.	Kansas City and Great Falls	Twin Cities	31	69
44.	Omaha and Billings	Twin Cities	32	68
45.	Omaha and Butte	Twin Cities	28	72
46.	Omaha and Great Falls	Twin Cities	29	71

[fol. 901]

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SECTION VII

	Between -	Interchange Points	Percentages MW	Percentages TC
1.	Wichita, Kans., and Seattle, Portland, San Francisco, Los Angeles	Kansas City	15	85
		Denver, Pueblo	27	73
2.	Wichita and San Francisco, Los Angeles	El Paso	39	61
3.	Wichita and Spokane, Reno, Las Vegas	Kansas City	17	83
		Denver, Pueblo	32	68
4.	Salina, Kans. and Seattle, Portland San Francisco, Los Angeles	Pueblo	25	75
5.	Salina and Spokane, Reno, Las Vegas	Pueblo	29	71
6.	Hastings, Nebr., and Seattle, Portland, San Francisco, Los Angeles	Denver	23	77
7.	Hastings and Spokane, Reno, Las Vegas	Denver	26	74
8.	Topeka and Seattle, Portland, San Francisco, Los Angeles	Denver, Pueblo	28	72
9.	Topeka and Reno, Las Vegas, Spokane	Denver, Pueblo	29	71
10.	Topeka and Boise	Denver	38	62
11.	Topeka and San Francisco Los Angeles	El Paso	41	59
12.	Topeka and Phoenix	El Paso	57	43
13.	Mitchell, S. Dak., and Seattle, Portland	Oakes, N. Dak.	16	84
		Aberdeen, S. Dak.	15	85
		Omaha	16	84
		Denver	30	70

[fol. 902]

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SECTION VII

	Between-	Interchange Points	Percentages MW	TC
14.	Mitchell and Spokane	Oakes	18	82
		Aberdeen	17	83
		Omaha	17	83
		Denver	31	69
15.	Mitchell and Los Angeles, San Francisco	Omaha	16	84
		Denver	31	69
		El Paso	44	56
16.	Mitchell and Reno, Las Vegas	Denver	40	60

[fol. 903]

	Between-	Interchange Points	Percentages MW	TC
1.	Memphis, Tenn. and Los Angeles and San Francisco	Kansas City	22	78
		Floydada	33	67
		El Paso	46	54
		Denver or Pueblo	39	61
2.	Memphis and Las Vegas, Reno	Kansas City	28	72
		Denver or Pueblo	47	53
3.	Memphis and Seattle, Portland	Kansas City	22	78
		Twin Cities	32	68
		Denver or Pueblo	38	62
4.	Memphis and Spokane	Kansas City	26	74
		Twin Cities	36	64
		Denver or Pueblo	42	58
5.	Memphis and Boise	Kansas City	47	53
		Denver or Pueblo	45	55
6.	Memphis and Phoenix	El Paso	58	42
7.	New Orleans, La. and Los Angeles, San Francisco	Kansas City	32	68
		Denver, Pueblo	43	57
		El Paso	46	54
8.	New Orleans and Las Vegas, Reno	Denver, Pueblo	53	47
		El Paso	50	50
		Kansas City	38	62
9.	New Orleans and Phoenix	El Paso	58	42
10.	New Orleans and Portland, Seattle	Kansas City	35	65
		Twin Cities	41	59
		Denver, Pueblo	46	54
		El Paso	39	61
11.	New Orleans and Boise, Spokane	Denver, Pueblo	52	48
		Kansas City	39	61
12.	New Orleans and Spokane	Twin Cities	47	53
13.	Little Rock, Ark. and Seattle, Portland, San Francisco, Los Angeles	Kansas City	23	77
		Denver or Pueblo	38	62
		El Paso	37	63
14.	Little Rock and Phoenix	Kansas City	26	74
		El Paso	54	46
15.	Little Rock and Las Vegas, Reno, Boise, Spokane	Denver or Pueblo	45	55
16.	Oklahoma City, Okla. and San Francisco, Los Angeles	Denver or Pueblo	29	71
		El Paso	39	61
		Floydada	20	80
		Kansas City	18	82

[fol. 904]

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SECTION VIII

	Between-	Interchange Points	Percentages MW	Percentages TC
17.	Oklahoma City and Seattle, Portland	Denver or Pueblo	29	71
		Kansas City	18	82
18.	Oklahoma City and Phoenix	El Paso	51	49
		Floydada	25	75
		Kansas City	22	78
19.	Oklahoma City and Spokane	Denver or Pueblo	34	66
		Kansas City	22	78
20.	Oklahoma City and Reno	Denver or Pueblo	37	63
		Kansas City	22	78
21.	Texas - Dallas/and Los Angeles, San Francisco	Kansas City	22	78
		Denver, Pueblo	31	69
		El Paso	34	66
22.	Dallas and Las Vegas, Reno	Denver, Pueblo	39	61
		Kansas City	27	73
23.	Dallas and Phoenix	El Paso	46	54
24.	Dallas and Seattle, Portland	Kansas City	22	78
		Denver, Pueblo	31	69
		El Paso	25	75
25.	Dallas and Spokane	Kansas City	25	75
		Denver, Pueblo	36	64
26.	Dallas and Boise	Kansas City	26	74
		Denver, Pueblo	39	61
27.	Texas - Houston and Los Angeles, San Francisco	Kansas City	29	71
		Denver, Pueblo	39	61
		El Paso		
28.	Houston and Las Vegas, Reno	Denver, Pueblo	48	52
		Kansas City	34	66
29.	Houston and Phoenix	El Paso	52	48
30.	Houston and Portland, Seattle	Kansas City	30	70
		Denver, Pueblo	39	61
		El Paso	31	69
31.	Houston and Boise, Spokane	Kansas City	33	67
		Denver, Pueblo	44	56
32.	Amarillo, Texas, and Seattle, Portland, San Francisco, Los Angeles	Denver or Pueblo	22	78

[fol. 905]

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SECTION VIII

	Between-	Interchange Points	Percentages MW	TC
33.	Amarillo and San Francisco, Los Angeles	Denver or Pueblo	22	78
34.	Amarillo and Phoenix	El Paso	40	60
35.	Amarillo and Reno, Las Vegas	Denver or Pueblo	28	72
36.	Amarillo and Spokane	Denver	25	75
37.	Amarillo and Boise	Denver	31	69

SECTION IX

Miscellaneous

The prescribed divisions shall not apply on traffic interchanged at Chicago by The Atchison, Topeka and Santa Fe Railway Company and the Chicago and North Western Railway Company subject to special divisions heretofore agreed upon by those carriers.

The divisions prescribed in Section V shall not apply on shipments to and from points on the line of the Wabash Railroad Company when it performs service both east and west of the Mississippi River, but in lieu thereof, the divisions prescribed in Section VI for the Chicago-Milwaukee-Peoria group shall apply.

Nothing in this report and order shall be interpreted as prescribing divisions of rates to and from points on the Durham and Winston-Salem districts of the Norfolk and Western Railway Company.

When intermediate switching service of the Terminal Railroad Association of St. Louis, the Alton and Southern Railroad, the Illinois Terminal Railway Company, or motor-carrier service is necessary to effect interchange at St. Louis or East St. Louis, the applicable charges for such service shall be payable from the eastern primary division on westbound shipments and from the western primary division on eastbound shipments.

[fol. 906]

[fol. 907] APPENDIX C

Rulings on Evidence

The defendants would have the Commission base its decision in part on purported facts discussed in their briefs but not proved as required by its General Rules of Practice and the Administrative Procedure Act. Not through witnesses but by tender of counsel they sought to introduce in evidence such matter as working papers collected by their cost analysts, a motion-picture film, and clippings of unsigned articles in trade journals. (In this course counsel departed from the ground rule agreed upon in prehearing conference under which evidence was reduced to writing and copies thereof with accompanying exhibits furnished to opposing counsel in advance of the hearing at which such evidence was offered.)

The consideration of this evidence by the Commission would be in violation of its General Rule of Practice 1.74, providing that "witnesses will be orally examined under oath before the officer unless . . ." [exceptions not pertinent here]. It would also be contrary to the following sentence in section 7(c) of the Administrative Procedure Act:

> Every party shall have the right to present his case or defense by oral or documentary evidence, to submit rebuttal evidence, and to conduct such cross-examination as may be required for a full and true disclosure of the facts.

The following comment on this section in the Attorney General's Manual on the Administrative Procedure Act, p. 77, is significant:

> As here used "documentary evidence" [28 U.S.C. 695] does not mean affidavits and written evidence of any kind. Such a construction would flood agency proceedings with hearsay evidence. In the last sentence of the subsection, there appears the phrase "evidence

> in written form," thus indicating that the Congress distinguished between "written evidence" and "documentary evidence. * * * Against this background, it is clear that the "right to present his case or defense by oral or documentary evidence" does not extend to presenting evidence in affidavit or other written form so as to deprive the agency or opposing parties, of opportunity for cross-examination. * * * Thus, technical and statistical data may be introduced in convenient written form subject to adequate opportunity for cross-examination and rebuttal. * * * Any evidence may be admitted by agreement or if no objection is made.

(Under the circumstances specified in the last sentence above quoted so-called counsel's exhibits are sometimes received but not otherwise.) The objectionable evidence for the most part was offered in the course of cross-examination of opposing witnesses for the purpose of controverting facts stated by those witnesses. Its exclusion by the examiners was not an interference with cross-examination, as argued, for it is well-settled that a party cannot introduce incompetent evidence in cross-examining an adversary witness. Nor were defendants entitled to demand that the objectionable material be numbered as an exhibit and incorporated in the record as permitted by Rule 1.84(e), which applies "in case exhibit has been identified" etc. An exhibit is a substitute for oral testimony "and should be limited to statements of fact." (Rule 1.84(a)). It receives its evidentiary status through identification by a witness and not by denomination of counsel.

[fol. 908] The matter referred to in the first paragraph above was offered after the defendants had completed their presentation while their opponents were exercising their right to close and was therefore out of order. This was also true of certain documents sought to be introduced, including an exhibit containing portions of records in other proceedings offered on the last day of the hearing but one.

The last-mentioned exhibit was "subject to objection." (Rule 1.82(d)). It was excluded on the ground that the complainants could not have exercised their right to rebuttal without unduly prolonging the hearing. Furthermore the rejected documents were similar to others already in the record and were therefore cumulative.

Likewise in the final stage of the hearings, which had then continued for more than 4½ years, the defendants filed with the examiners a motion for issuance of *subpoena duces tecum* directing an eastern railroad to produce certain wheel reports, represented as being helpful to the Commission in reaching its decision. No right on the part of the defendants to the use of this material at that stage of the proceedings was asserted in the motion. The examiners denied the motion in the exercise of their discretionary powers, and the defendants now claim that they were prejudiced by that action. The material sought would have been voluminous and of doubtful relevance. To have required its production would have greatly prolonged the hearings, and the motion was properly denied.

[fol. 909]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Transcontinental Divisions Cases

No. 31503 and Sub Nos.

THE AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY et al.,

vs.

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY et al.

EXCEPTIONS OF MOUNTAIN-PACIFIC RAILROADS TO RECOMMENDED REPORT

S. R. Brittingham, Jr., R. Granville Curry, Frank S. Farrell, Lawrence W. Hobbs, Thormund A. Miller, Ernest Porter, Howard V. Rhedin, L. E. Torinus, Jr., E. L. Van Dellen, Howard J. Trienens, Douglas F. Smith, Counsel for the Mountain-Pacific Railroads.

Due Date: April 5, 1961.

Oral Argument Is Requested

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[fol. 910]

Foreword

* * * * * * *

[fol. 911] In hearings extending over a period of more than four years, the contesting parties compiled the large exhaustive record which they believed necessary to a proper determination of the issues under the standards of Section 15(6) of the Act and the precedents of the Commission and

the courts. Following the hearings and the filing of briefs, the Examiners who heard the case submitted the Recommended Report here under consideration.

No doubt the Examiners have earnestly endeavored to reach a proper decision in this case. However, when their report is dispassionately appraised, it is believed fair to say that it contains such startling misconceptions of the principles to be applied, such erroneous assumptions on the basis of material outside the record, such failure to make vital and necessary findings, and such severely unjust and unwarranted transfers of revenues as to destroy any presumption which might otherwise arise from a recommended report, and utterly to invalidate the conclusions reached.

The most extraordinary feature of the Recommended Report is that it is not based upon the record made by the parties but upon a new issue, created by the Examiners using passenger deficit data outside the record. Also, strikingly apparent is the avowed failure to make findings on the primary cost issues to which the major part of the record was directed. Even as to the so-called revenue needs issue, the Examiners do not rest their conclusions on the actual reported earnings of the carriers. Their recommendation is, instead, predicated upon the hypothetical creation of some $60 million of additional revenue annually for the Mountain-Pacific lines through the elimination of asserted inefficiency in their passenger operations. This $60 million in annual revenues is created both to supply the source of funds from which the documented revenue needs of the Mountain-Pacific lines are to be met and to provide the money to pay the increased transcontinental divisions recommended for the Official and Midwestern lines.

* * * * * * *

[fol. 912] The extreme character of the increases in the percentage divisions of the Official and Midwestern lines, and the magnitude of the present revenues to which such divisions would apply, make it apparent that the transfer of revenues recommended by the Examiners is vast and

staggering. But the remarkable fact is that no amount is stated in the report as the increase to be allotted to the Eastern or the Midwestern roads, how such sum would compare with present divisions, or what the effect of the transfer would be on the roads involved.***

* * * * * * *

[fol. 913]

Specific Exceptions

Exception No. 1—To the Examiners' New Charge that the Mountain-Pacific Roads are Inefficient in Their Passenger Operations, a Charge Devised to Create Funds for Transfer to the Official and Midwestern Roads.

In its one dominant feature this is undoubtedly the most extraordinary Recommended Report ever submitted to the Commission. On a record of the broadest scope, laboriously compiled over a period of four years by three groups of roads in support of their respective claims for increased divisions, the Examiners found nothing to sustain a change in the present divisions which have been in effect for a generation. The status created by the record was deemed by them to be one of stalemate. The parties had labored prodigiously but brought forth nothing decisive. Thereupon, after the close of the record, the Examiners, drawing upon data outside the record, came forward with a single, simple table of "Passenger Deficits—1948 to 1959" (sheet 28).* This was made the axis on which the whole case revolves under the recommended report.

*** If the recommended transfer were actually based upon the "revenue needs" ground sanctioned by the Act, i.e., an identified public requirement, a measure of the sum involved would necessarily be inherent in the basic determination. But the proposal to transfer an unknown sum on that ground is self-contradictory since it permits no knowledge whether the overall public interest has been helped or hurt.

* At sheet 27, the Examiners state that they "take official notice" of various data for individual roads and groups of roads. Such

The cost studies were cast aside, without "attempting meticulously to unravel the tangled skein of controversy" (sheet 19), as posing problems for "neutral technical experts" (sheet 15); the revenue needs evidence, as shown by existing actual earnings, was deemed to be indecisive. Apart from certain fringe observations and conclusions, the record, as made by the parties, was disposed of in this summary fashion. The drastic affirmative action recommended, the enormous shift of revenue which is proposed, [fol. 914] rests solely upon the imaginative creation of a fund to be derived by the Mountain-Pacific roads from a reduction of their passenger deficits. It is from such a fund that the Mountain-Pacific roads are to meet their own undisputed, pressing public requirements for additions and betterments, and also to pay the recommended higher divisions to the Midwest and East. Both the method and the result are without precedent.

A. The Evidence Showing the Need for Larger Revenues to Serve Mountain-Pacific Territory.

The critical evidence on the practical and pressing need of the Mountain-Pacific lines for funds arises from the compelling public pressure on those roads to expand their railroad plant to meet the transportation needs of the nation's fastest growing territory. The Official and Midwestern roads have the very different problem of administering

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data appear at sheets 28 and 32, including footnotes at pages 2-4 of Appendix A to the report, and are discussed at other sheets of the report as well.

No notice was given that these data, or the contentions based upon these data, were to be used in this proceeding. In *United States* v. *Abilene & So. Ry. Co.*, 265 U.S. 274, 290, the Supreme Court ruled:

> "The general notice that the Commission would rely upon the voluminous annual reports [and even such a general notice was not given here] is tantamount to giving no notice whatsoever. The matter improperly treated as evidence may have been an important factor in the conclusions reached by the Commission. The order must, therefore, be held void."

stable or shrinking transportation plants. The highlights of the evidence on this critical subject include the following facts:

The Mountain-Pacific lines have experienced the greatest growth of population in the territory served and the greatest increase in the physical volume of traffic (ton miles) and gross freight revenues, as the Examiners find (sheets 20-21).

Practically the entire increase in the traffic volume of the Mountain-Pacific roads has been concentrated in commodities subject to market competitive forces unique to the transcontinental hauls and resulting in severely depressed rates which have been further depressed by the series of "holddowns" authorized and imposed by the Commission in general rate increases.*

To handle their increased volume of traffic, the Mountain-Pacific lines have increased their net investment in transportation plant by $1½ billion over the post-war period, 1947-1957, but far from receiving a fair return on that added investment, the owners of the property received no additional return whatever on the additional investment.** [fol. 915] Similarly, in the five years 1951-1955, the Mountain-Pacific lines increased their net investment in railroad property by $800 million but this increase in investment produced not one penny of increased earnings, as the Examiners state (sheet 30).

Taking account, on the one hand, of all funds available from their transportation operations, and, on the other, of the funds devoted to transportation operations and plant over the same period 1951-1955, the balance available for the stockholders of the Mountain-Pacific lines was only $46

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* Exhibit T-294, pp. 3-5 and App. A.

	Net Investment	NROI Adj.
** 1947 (Exhibit T-238, p. 17)	$5,237,446,107	$203,420,031
1957 (Exhibit T-652, Appx. A, p. 2)	6,786,828,226	202,430,921
	+$1,549,382,119	—$ 989,110

million, or 1.07% of the stockholders' investment in transportation property. The Official and Midwestern lines produced funds available for their stockholders during the same period at the rate of 1.40% and 1.79%, respectively.*

Quite apart from any considerations of fairness to the owners of the properties, the public interest in protecting and augmenting these slim returns is plain. This is of special importance to this case because these marginal returns are obtained under the present transcontinental divisions upon which the Mountain-Pacific lines depend for half of their freight revenues. Furthermore, even this marginal return is now substantially extinguished with the expiration of federal income tax deferrals.

The Examiners concede, as did all the parties, the principle that temporary tax deferrals overstate earnings data of record, and they note that this affects the "western lines principally" (sheet 27). But the Examiners fail to find that the earnings of the Mountain-Pacific lines are overstated in substantially greater degree than the earnings of the Midwestern as well as of the Official lines (Exhibit T-652, pp. 4-5). Most important, the Examiners fail to relate the elimination of this temporary overstatement of earnings of the Mountain-Pacific lines to their ability to obtain the funds necessary to meet the service demands of Mountain-Pacific territory.**

The Recommended Report cannot and does not challenge these uncontrovertible facts. The need of additional revenues to meet the transportation requirements of the public in Mountain-Pacific territory is not questioned. The $800 million in added investment in railroad plant in the period [fol. 916] 1951-1955 and one and one-half billion dollars in the period 1947-1957, is unchallenged, as is the startling fact that the owners of the properties received not one penny of return on the vast added investment (sheet 30).

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* Exhibit T-275, p. 2. The relationships are substantially the same over the entire post-war period (Exhibit T-275, pp. 3-4; Exhibit T-659, Appx. G).

** As discussed at pages 142-143 and 180-182 of our Brief.

Faced with such facts, the Examiners could not and do not recommend a reduction of our lines' divisions on the basis of the record before them. The Examiners go outside the record to create funds from which they assume that the Mountain-Pacific lines could absorb reductions in divisions.

B. The New and Untenable Charge of "Excessive Passenger Deficits," Based on Theories Previously Rejected by the Commission.

The passenger deficit dictum was put forward by the Examiners to avoid the uncontroverted evidence showing the need of the Mountain-Pacific roads for more revenues to serve their territory. Confronted with this indisputable fact "that 'the increased investment required in serving the growing Mountain-Pacific territory has produced no return for the owners'" of the roads, the Examiners assert: "This alleged deprivation results from excessive passenger deficits of those roads as will now be explained" (sheet 30).

The Examiner's method is to use the passenger deficits in 1948 as the standard or norm relationship as between Official and Western roads and then, in the ensuing period of years, assume the same passenger train conditions in both territories. On that basis alone, the Examiners find that the "annual savings", meaning "enhanced earnings", of the transcontinental lines "would have been more than $60 million per year" if they had the same passenger deficit experience as the Official lines since 1948 (sheet 28 and fn 15). Only by creating those funds through an assumed reduction in the passenger deficit are the Examiners able to answer the critical question asked by the state commissions. The report states (sheets 30-31):

> "The intervening State Commissions share the defendants' concern as to whether those railroads can obtain necessary funds to increase their facilities to the extent necessary to keep pace with the expanding economy of the mountain-Pacific States. One of the interveners' briefs has the following to say on this point:

> In spite of the pressing need for additional investment in equipment and transportation facilities, the mountain-Pacific carriers cannot look to rate increases to provide increased earnings but instead [fol. 917] must face further rate reductions. Where then is the money necessary to provide additional facilities, and to maintain the earnings of the Mountain-Pacific carriers to come from?"
>
> * * *
>
> "The obvious answer to the question stated in the foregoing quotation is that a reduction in the passenger deficit of the mountain-Pacific lines, which would seem to be imperative sooner or later, should help materially in furnishing funds for additions and betterments. The interveners are in a position to assist in such a course by taking a sympathetic attitude toward discontinuance of unprofitable passenger service."

The Examiners thus rely upon funds to be created by a supposed reduction of the passenger deficit to deny to the Mountain-Pacific roads increased divisions which are otherwise necessary to meet public demands for service. The Examiners also would use these hypothetical funds to finance the vast transfer of divisional revenues to the Midwestern and Eastern lines which they recommend.

The Examiners concede that the six Mountain-Pacific lines which they selected (Santa Fe, Rio Grande, Great Northern, Northern Pacific, Southern Pacific and Union Pacific) are devoting hundreds of millions of dollars of additional investment to serve the transportation needs of Mountain-Pacific territory. That the owners of those railroad properties have been deprived of any actual return on their added investment is also conceded. But the Examiners would avoid these facts by finding that these roads can become as efficient in the operation of their passenger business as the Pennsylvania, the New Haven and the other Official lines and that they will then have ample revenues to cure this "deprivation" (sheet 30), have additional funds

for investment (sheet 31), and also have funds to transfer vast amounts to the Official and Midwestern roads through the increased transcontinental divisions recommended by the Examiners.

This is all fantasy. There is no such fund of 60 million dollars per year waiting for the Mountain-Pacific lines to tap. This charge of "excessive passenger deficits" is a brand new issue, created by the Examiners for the first time in their recommended report. As we shall show, it is based on a series of untenable assumptions which improperly bring into this case controversial views on passenger deficits already rejected by the Commission in a separate investiga- [fol. 918] tion dealing specifically with that subject. The Examiners themselves invent the issue of inefficiency in passenger operations and create the record from which it is derived,* as follows (sheets 27, 28):

Passenger Deficits (Thousands)

Year	Eastern District and Pocahontas Region	Western District	Transcontinental Lines (AT&SF, D&RGW, GN, NP, SP, UP)
1948	$252,145	$234,625	$107,492
Average 1949-1959	$243,895	$309,494	$164,419
Percentage Change, 1948 to average 1949-1959	—3%	+32%	+53%

* None of the group passenger deficit data relied upon by the Examiners was in the record. The only passenger deficit data of any kind in the record consisted of certain individual road figures included in an exhibit introduced by a Midwestern lines' witness at the last hearing; far from forming the basis for any charge of excessive deficits on the Mountain-Pacific roads, the passenger deficit data was incidental to other data used in claiming that the C&NW passenger operating ratios were no worse (and no better) than those of other roads in the West. (Exhibit MW-738, pp. 37-38 and Appx. B).

The Examiners conclude (sheet 28):

> "If the rail carriers in the western district had been able to hold their average annual passenger deficit in 1949-1959 to a figure 3 percent less than their 1948 deficit, their revenue saving would have been nearly $82 million per year. The annual saving of the transcontinental railroads similarly estimated would have been more than $60 million per year."

This is the source and the sole documentation of the charge of "excessive passenger deficits of these [transcontinental] roads" (sheet 30). It is by reliance on these figures that the Examiners undertake to create the $60 million in funds to meet the transportation needs of Mountain-Pacific territory and, at the same time, to pay out vast sums of divisional revenues to the Official and Midwestern roads.

To reach the conclusion from these figures that the passenger deficits of the Mountain-Pacific roads are "excessive," the Examiners must of necessity make a series of underlying determinations or assumptions, including these:

1. That the returns from passenger operations in the East since 1948, a selected base year, constitute a [fol. 919] reliable gauge and measure of efficiency in the conduct of the passenger operations of the transcontinental lines;

2. That the passenger traffic, facilities, service and operations in the East, in 1948 and thereafter, were comparable to the passenger business in the territory served by the transcontinental lines;

3. That the extensive passenger train discontinuances inherent in the Examiners' conclusions would be approved by the States or by this Commission, without reference to the specific facts of record in the individual proceedings and the consideration by these tribunals of the public need for the service;

4. That such train discontinuances would produce, not merely reductions in a statistical deficit, but actual dollar savings of $60 million or more annually; and,

5. That the potential for future dollar savings is greater for the transcontinental lines than for the Official lines.

Each of these underlying issues has necessarily been decided by the Examiners in reaching their ultimate finding of the existence and measure of the Mountain-Pacific roads' "excessive passenger deficits" relative to the Official lines. Determination of such highly controversial issues inherent in a new charge of this character, based on evidence outside the record, denies the full and fair hearing required under the Act and by due process of law. The Supreme Court so ruled in *Interstate Commerce Commission* v. *Louisville & N.R.R.*, 227 U.S. 88, 93:

> "All parties must be fully apprised of the evidence submitted or to be considered, and must be given opportunity to cross-examine witnesses, to inspect documents and to offer evidence in explanation or rebuttal. In no other way can a party maintain its rights or make its defense."

The Examiners' creation of the new charge of "excessive passenger deficits," on the basis of figures outside the record and the determination of the controversial issues listed above, would, at the very least, require a hearing at which our lines would have the opportunity to "offer evidence in explanation or rebuttal." The nature of the evidence which would be offered at such a hearing is briefly summarized in Appendix II attached to these Exceptions. As shown in Appendix II, each of the underlying issues listed above has [fol. 920] been erroneously and improperly decided by the Examiners on the basis of superficial and extremely misleading statistics.

However, it is neither necessary nor proper that the Commission undertake to resolve in this transcontinental

divisions proceedings numerous and highly collateral questions as to passenger deficits. The Commission has only recently completed an extensive separate investigation, *Railroad Passenger Train Deficit,* 306 I.C.C. 417, in which it considered many of the issues underlying the Examiners' finding of "excessive passenger deficits" here. In its report in that proceeding, the Commission squarely rejected the opinions of its Examiner, who was also the Presiding Examiner in this divisions proceeding. The following table contrasts the findings proposed by the Examiner in the *Passenger Train Deficit* case with the Commission's findings on the same issues:

Docket 31954, Examiner's Proposed Report	Commission Report (306 I.C.C. 417)
"For more than a century the railroad passenger coach has occupied an interesting and useful place in American life, but at the present time the inescapable fact—and certainly to many people an unpleasant one—seems to be that in a decade or so this time-honored vehicle may take its place in the transportation museum along with the stagecoach, the sidewheeler, and the steam locomotive."	
• • •	
"If railroad passenger-miles (other than commutation) continue to decline at the average rate of reduction between 1947 and 1957, the parlor and sleeping-car service will have disappeared by 1965 and the coach service by 1970." (sheet 69)	"There has been considerable and perhaps undue emphasis on statistical trends interpreted as a portent of the eventual disappearance of [passenger] service within 10 or 12 years, if railroad passenger-miles (other than commutation) continue to decline at the average rate of reduction between 1947 and 1957." (p. 479)

Docket 31854,
Examiner's Proposed Report
(Cont'd)

"The I.C.C. receives numerous letters from critics of the railroads as well as sincere well-wishers who would like to see their passenger service continued. These writers usually urge that the railroads run more trains with improved equipment, serving less expensive and better meals, and charging lower fares. Sometimes they accuse the railroad executives of wanting to get rid of their passenger busi-
[fol. 921]
ness regardless of its profitability and charge that the passenger deficit is a kind of phantom produced by archaic or dishonest accounting.

"These are mistaken ideas.
* * *

"Few, if any, railroads are in a financial position to experiment on a large scale with new kinds of passenger motive power and equipment. Such experiments would be questionable in view of the contracting share of the travel market available to the railroads today." (sheets 71-72)

Commission Report
(306 I.C.C. 417) (Cont'd)

"Nonetheless, the record and our correspondence clearly disclose that many avenues toward improving the attractiveness of railroad passenger service remain unexplored. The aggressive service policies of competitors for the travel market in a day of rapid technological and marketing innovations must, at least, be counterbalanced with equally progressive railroad policies. (p. 481)

* * *

"Specifically we recommend:

* * *

"7. That experimentation by the railroads with new types of coaches, sleeping cars, dining and other facilities be continued.

"8. That railroad management should continue its efforts to improve the attractiveness of railroad passenger service as a means of stimulating more adequate volume of traffic." (pp. 482, 483)

* * *

"We are of the view that the complete elimination of passenger-train service would not be a solution in the public interest. Economic railroad passenger service is, and for the foreseeable

Docket 31854, Examiner's Proposed Report (Cont'd)	Commission Report (306 I.C.C. 417) (Cont'd)
	future will be, an integral part of our national transportation system and essential for the Nation's well-being and defense" (p. 484)
"The passenger deficit is not something which can be conjured away by statistical legerdemain. It is real and serious." (sheet 72)	"The separation rules do not reflect, nor are they intended to provide, the cost of operating individual trains; they are not intended to determine the expenses which would be avoided if all passenger services were discontinued; and they are not intended to measure the elusive 'out-of-pocket' costs." (p. 427)

The Examiners' treatment of the passenger deficit issue which they have created and injected into this divisions case reflects the views expressed in the Examiner's report in the passenger deficit investigation and subsequently rejected by the Commission. Thus, the Examiners here equate a reduction in the statistical passenger deficit with an "annual saving", meaning "enhanced earnings" (sheet 28 and fn 15), which "should help materially in furnishing funds [fol. 922] for additions and betterments" (sheet 31). The Examiners consider that "discontinuances of unprofitable passenger service" will produce such funds (sheet 31), thereby confusing the statistical passenger deficit with the very different question whether discontinuance of trains will produce such actual dollar savings (as discussed in our Appendix II). And, most significantly, the Examiners assume that such discontinuances and resulting reduction in passenger deficits "would seem to be imperative sooner or later" (sheet 31). It is apparent that the Presiding Examiner is of the same opinion still, notwithstanding the Commission's rejection of his views in the *Passenger Train Deficit* Investigation.

Thus the Commission has already rejected, in a proceeding directly concerned with passenger service and deficits, the new and untenable charge of "excessive passenger deficits" upon which the Examiners have based their recommended divisions.

C. The Examiners' Failure to Consider Evidence as to the Tremendous Potential for Actual Dollar Savings from Extensive Mergers and Consolidations.

The Examiners' excursion outside the record to find a "potential" of increased funds through elimination of "excessive passenger deficits" is to be contrasted with their refusal to consider the great potential of increased funds available through mergers and other means of eliminating duplicate facilities which are now in formulation, being heard, or already approved and in the process of consummation.

The Commission has recognized the vast potential for savings in the merger and consolidation of railroad properties. The Chairman of the Commission recently testified before Congress:*

> "The second method of producing efficiency and economy [apart from 'technological and mechanical improvements'] is through the elimination of waste. This takes many forms: Elimination of duplicating facilities, multiple yards and terminals causing expensive interchange operations and excessive loss and damage claims, internal reorganizations, consolidations, pooling of traffic, standardizing equipment, etc. Items of this kind have not been fully exploited. They are highly productive in promoting more net on the same gross [fol. 923] revenues, yet the advantages of aggressive efforts in this direction have not been fully utilized.
>
> * * *

* Testimony of Chairman Freas, Hearings before Senate Committee on Interstate and Foreign Commerce, "Problems of the Railroads", 85th Cong., 2d Sess., pp. 1845-1846, 1847.

"We believe that, where consolidations of railroads would produce substantial economies without sacrificing service to shippers or otherwise affecting the public interest adversely, they should be encouraged." *

* See also the remarks of Commissioner Tuggle, 72d Annual Convention, NARUC, November 30, 1960, "The Outlook for Railroad Consolidations and Mergers", pp. 4-5, 6, 8 and 17:

"One facet of the financial plight of the Nation's railroads may be illustrated from the Ex Parte 223 proceeding: Since January 1, 1958, the *yearly* increased fixed expenses for all Class I railroads amounts to $607.7 million which is $460.9 million more than the estimated increase in revenues of $146.8 million, from the increased rates proposed in that case. The increased expenses cannot be avoided since they result from higher material prices, wages, payroll taxes, and mileage rates on private-line cars. How can this additional annual burden of $460.9 million be met?

"One obvious answer is through operating economies generally. In my judgment there are two principal ways to accomplish this: (1) mergers consistent with the public interest and (2) new equipment and techniques. Number 2 costs money because modernization of rail facilities comes high. But mergers can make a substantial contribution to revenues as well as more efficient services. The benefits that would flow from sound mergers of railroad properties are evident, and in my opinion necessary to accomplish the modernization of the railroad plant.

* * *

"I refer to the many situations throughout the country where consolidations of railroads would produce substantial economies, thereby contributing greatly to the financial needs of the industry. In many large cities there is unnecessary and wasteful duplication of expensive railroad terminal facilities, both freight and passenger, and highly taxed.

* * *

"I think we can agree that there are many situations where the public interest does not require several sets of tracks, with all of the attending facilities that go with them, owned or operated by different railroads, between the same terminal areas. This is particularly true as to parallel competing rail lines which serve substantially the same intermediate territory.

* * *

"In conclusion, and for the record, I want to say that the Interstate Commerce Commission stands ready, willing, and able—and I might add anxious—to give thorough and sympathetic consideration to any merger proposals under section 5."

[fol. 924]

RAIL NETWORK OF THE
UNITED STATES

Source: Exhibit MW-117, Appx. B.

[fol. 925] The Senate Committee before which the Commission's position was thus stated responded by stating in its report:*

> "The railroad industry has not, in the subcommittee's opinion, been sufficiently interested in self-help in such matters as consolidations and mergers of railroads; joint use of facilities in order to eliminate waste, such as multiple terminals and yards that require expensive interchange operations; reduction of duplications in freight and passenger services by pooling and joint operations;"

The utter certainty, neglected in the Examiners' report through their preoccupation with comparative passenger deficits, is that the railroads are in the process of a fundamental realignment of properties. A new map is being drawn, and any divisions prescribed in this case will be effective under conditions totally different from those shown in this record.

The merger movement is now being progressed in all territories, but its primary impact and benefits will inevitably be felt in those territories where the greatest duplication of facilities currently exists. A glance at the map of the rail network in this country, reproduced on the opposite page (now p. 809), makes it clear that the greatest concentration of duplicating lines and facilities is in the East and in the Midwest east of the Missouri River. The Midwestern lines' witness concluded from this map: "There being so many available routes in the Midwestern territory results in a diffusion of traffic, thereby reducing volume and increasing costs." (Exhibit MW-117, p. 6.)

The potential for savings is even greater in Official territory. As stated in the application of the Erie and Lackawanna (Application in Finance Docket 20707, p. 35):

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* Report of Subcommittee on Surface Transportation, Senate Committee on Interstate and Foreign Commerce, 85th Cong., 2d Sess., dated April 30, 1958, p. 5.

> "Elimination of duplicate facilities and other reductions in expenses which can be achieved by a merger are especially important in the case of railroads, such as the Applicants, which have proportionately heavy terminal expenses and property taxes."

The Commission recently approved the Erie-Lackawanna merger, expected to produce savings of $13,500,000 annually, [fol. 926] 312 I.C.C. 185, 186, 213, 244, 237. The Commission previously approved the Norfolk & Western-Virginia merger designed to produce annual savings of $12,000,000, 307 I.C.C. 401, 424-425. Other merger actions proposed by Official territory lines include the application of the Norfolk & Western and Nickel Plate to merge (Finance Docket 21510) and to control the Wabash (Finance Docket 21511), and some combination of the C&O, B&O and Central. (See Application of NYC to acquire B&O, Finance Docket 21237, and Application of C&O to acquire B&O, Finance Docket 21160.)

The magnitude of the savings as yet unrealized within Official territory is indicated by the Pennsylvania's Vice President, Finance, in his description of the proposed Pennsylvania-New York Central merger:

> "Finally, with respect to consolidations, unfortunately our so-called 'Marriage' with the New York Central collapsed. I guess you might say we were the bride-to-be left waiting at the altar. We were deeply regretful since in our judgment there was an annual savings potential of $100 million involved." *

The Mountain-Pacific lines are also progressing mergers or consolidations to realize such savings from this source

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* Exhibit T-691, Sec. A, p. 8. The authenticity of this statement was conceded by counsel for the Pennsylvania (Tr. 9619), but the exhibit was excluded by the Examiners and improperly so for the reasons set forth at pages 140-142, of these Exceptions, *infra*.

as can be obtained,* but it is obvious from the map of the rail network in this country that the Mountain-Pacific lines have no such great potential for savings through elimination of duplicate facilities as exists between the Missouri River and the Atlantic Seaboard. With this great potential now being tapped through a series of pending and proposed mergers, this period of radical change and general ferment is a most incongruous time to upset a divisional structure that has been in effect for a generation on the ground of a supposed potential for savings in passenger operations. Unlike the statistical passenger deficits for our lines, which include common costs that must be incurred in any event for the freight service, the potential in mergers, disregarded by the Examiners, means actual dollar savings.

[fol. 927] The Examiners do not mention at all in their report the duplicate facilities of the Eastern roads. In fact, the Examiners make findings which are in exactly the opposite direction. Of the factors discussed under the heading "Revenue Needs," the Examiners give special emphasis to the increasing population of the Mountain-Pacific states (sheet 20,** and the increasing volume of traffic of the Mountain-Pacific lines, measured in Revenue Ton Miles (sheets 20-21). The Examiners state "even more significant than a comparison of rates of return is the post-war trend of declining freight traffic of the eastern railroads shown in this record." (sheets 31-32). The Examiners' basic error is not in the facts as to the trends in the physical volume of freight handled, but in the bearing those facts have on the revenue needs issue in this divisions case.

The increase in revenue ton miles experienced by Mountain-Pacific lines has required vast additional investment to provide transportation service. The increased revenue

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* Great Northern and Northern Pacific, Application in Finance Docket 21478; Southern Pacific or Santa Fe and Western Pacific, Applications in Finance Dockets 21314 and 21334.

** The Examiners have again gone outside the record to obtain the 1960 census data shown at sheet 20.

ton miles, however, have been predominantly in traffic moving at rates severely depressed by market competitive forces and further depressed by "holddowns" prescribed by the Commission in general increase cases. These rate "holddowns" operate most drastically on the longest hauls, namely the transcontinental traffic upon which the Mountain-Pacific lines depend for their revenues.* This explains why the Mountain-Pacific roads have not received one penny of return on the billion and a half dollars of their added investment in transportation plant, as discussed at pages 18-20, *supra* (now pp. 796-799). The Mountain-Pacific lines thus have the burden of growth, in the requirement of added investment to handle the added business, but without any growth in earnings to provide any return on the added investment (Exhibit T-659, pp. 27-28). Since the Mountain-Pacific lines depend upon the transcontinental traffic for half of their freight revenues, a change in the divisions on this traffic is of vital consequence to the revenue needs of those lines.

[fol. 928] The Eastern and certain Midwestern lines, on the other hand, are experiencing a contraction in the traffic for which their lines were built. If they undertake to handle such a declining volume of ton-miles without contracting their railroad plant, the average costs per unit of traffic necessarily increase disproportionately and their earnings decline.** It is because of the decline in traffic and the exist-

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* The effect of "holddowns" and the forces depressing the revenues on the traffic available to the Mountain-Pacific lines, established by the uncontroverted evidence discussed at pages 155-172 of our Brief, is completely disregarded by the Examiners.

** See, for example, the Recommended Report of Commissioner Webb and Examiner Ries in Docket 33332, The New York, New Haven, and Hartford R. Co. (sheet 9):

> "It would seem that the New Haven's problem is to isolate those operations that show some promise of economic vitality and abandon those operations where no such promise now exists. That is to say, shrink the system on a functional basis.
>
> "Little effort has been made in that direction. For example,

ence of duplicate facilities and other burdens of overcapacity that the merger movement is so important to the Eastern and Midwestern roads. The Examiners, however, draw the wrong conclusion from the declining traffic of those lines. Without any comparison or recognition of the very different revenue needs problems of growing and contracting railroad plants, indeed without any rationalization at all, the Examiners conclude that the transcontinental divisions should be increased for roads experiencing declining ton miles.

The Examiners go outside the record to find an artificial potential for savings in passenger deficits, but they give no recognition to the potential in the elimination of duplicate facilities which lies at the heart of the revenue needs problem of important Eastern and Midwestern roads. They also fail to recognize the practical fact that transcontinental traffic is of only incidental importance to the financial condition of the Eastern and Midwestern roads since it constitutes but 5% and 15%, respectively, of their freight business (and less than 5% for the New England roads) (Exhibit T-311, pp. 8, 9). As a result, any change in the transcontinental divisions of the Eastern lines would provide only a minor palliative which could only delay and divert attention from the real solution of the problems of those lines.

In summary, the Examiners venture outside the record to avoid the force of the evidence establishing the inadequacy of the returns and funds available to the Mountain-Pacific roads. On the basis of their own submission, the [fol. 929] Examiners make the new charge of "excessive passenger deficits" in order to create funds for our roads through the elimination of the asserted inefficiency while, at the same time, ignoring the much greater potential of

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in the last ten years the New Haven has abandoned only fifty miles of line and, in the years 1951-1959, only thirty miles. The shrinkage, such as there has been, seems to have been done reluctantly, belatedly, and on a piecemeal basis."

actual dollar savings through mergers and elimination of duplicate service in the East and Midwest. This charge is an insistence upon views of passenger deficits which have already been rejected by the Commission in the proceeding brought specifically to deal with such issues. The Examiners' assumptions underlying their charge would, if relitigated in this divisions proceeding, necessitate an extensive hearing which would only establish again the fallacies of the Examiners' views, for the reasons summarized in Appendix II hereto.

This divisions case should be decided on the basis of the ample record now before the Commission, not on collateral and untenable assumptions regarding passenger deficits which already have been authoritatively rejected. In defaulting a resolution of the dominant cost of service and revenue needs issues, on the basis of the record actually before the Commission, and then going outside the evidence to create and decide an issue on which there was no hearing, the report plainly recognizes the stubborn fact that the record made does not support any order reducing the divisions of the Mountain-Pacific lines but, instead, justifies and requires an increase in the divisions of those lines.

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[fol. 930]

Exception No. 6—To the Examiners' Use of an Unlawful Standard of "Revenue Needs" and Failure to Make the Findings Essential to Action on this Ground.

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A. The Use of An Unlawful Standard of "Revenue Needs."

The report makes it plain that the Examiners apply the "revenue needs" test as requiring no more than a cryptic statement of "financial disparity" (sheet 34), based on a comparison of the relative "earning power" of the respective groups of railroads (sheet 33). This is an unlawful test. The Act does not contemplate or sanction the mere equalization or socialization of earnings and returns to the

owners of different railroad properties through the medium of a transfer of divisional revenues. "Revenue needs" justifies a change in divisions only if such a change is required in the public interest in order to maintain carriers "in effective operation as part of an adequate transportation [fol. 931] system." *New England Divisions*, 260 U.S. 184; *United States* v. *Abilene & S. Ry. Co.*, 265 U.S. 274, 280, 284-285; *United States* v. *Great Northern R. Co.*, 343 U.S. 562, 575-576.

The Examiners accord only verbal recognition to this test. They assert, only with respect to the Eastern roads, that the divisions of those roads should be increased in consideration of "the requirement of the public interest that all essential parts of the transportation system be maintained, so far as possible, in effective working condition." (sheet 34). This, however, is a mere statement of ultimate conclusion. It is entirely without support of essential underlying findings of fact, including:

(a) a finding identifying the particular transportation needs which it is necessary to protect by means of a transfer of divisional revenues;

(b) a finding of the amount of revenue necessary to accomplish the objective required by the public interest;

(c) a finding of the effect of the transfer of such an amount of revenue upon the transportation needs of the public served by the roads from which the divisional revenues are taken.

No such findings are to be found in the Examiners' report. No rational findings underlying a change in divisions based upon revenue needs could be made without knowledge of the amount of revenues that would be transferred under the recommended divisions.

A transfer of revenues based exclusively on proof of the parties' relative cost contributions to the service per-

formed, and not in any degree involving the public interest, may presumably be ordered whatever the amount. On the other hand, when the costs are not determined, and the transfer rests solely, as proposed here, upon the dominant interest of the public in the maintenance of a necessary transportation service, it must be known what the public need is in both territories, and whether a specific transfer from one group to the other will, on balance, help or hurt the overall public interest.

An increase in the transcontinental divisions of all Official lines as recommended by the Examiners is a most inefficient and defeating mechanism for dealing with revenue needs, since the C&O, Nickel Plate, Wabash and other relatively prosperous roads would, receive a larger [fol. 932] share of the increased divisions than such roads as the New England group whose low earnings depress the Official territory average. Thus, out of every $1000 of additional revenue received by the Official lines, the C&O would receive $48 while the Boston & Maine received $9, the Wabash would receive $92 and the Nickel Plate $79 while the New Haven received $19 (sheet 5).

And, most significantly as to the Official lines as a whole, transcontinental traffic constitutes but 5% of the total freight traffic of those roads, so that any change, however drastic, could have relatively little effect on the overall financial condition of the Official roads and their ability to serve the public. For the Midwestern lines, only 15% of their total freight revenues are derived from transcontinental traffic. At the same time that the increase in transcontinental divisional revenues, would be spread out among the Official and Midwestern roads, the full brunt of the transfer of revenues would fall on the seven principal Mountain-Pacific roads who are dependent for half of their total freight revenue on these divisions. The ability of those roads to serve the rapidly growing Mountain-Pacific territory would be impaired entirely out of proportion to the benefit to the total operations of roads in the East and

Midwest to whose financial condition the transcontinental traffic is of incidental importance only.

The Examiners note these critical relationships in another context (sheet 12), but entirely disregard their important bearing upon revenue needs. The significance of the relative importance of transcontinental traffic to the respective groups is that a transfer of divisional revenues from the Mountain-Pacific lines to the Official lines would seriously impair their overall financial condition and ability to serve the public without producing any substantial improvement in the financial position of the Official lines. Conversely, an increase in the transcontinental divisional revenues of the Mountain-Pacific lines would materially improve the ability of those lines to meet their growing service requirements without materially affecting the system earnings of either the Official or the Midwestern lines that depend primarily on other traffic for their revenues.

The practical situation is, then, that transcontinental revenues are the lifeblood of the Mountain-Pacific lines and yet, without recognition of that fact, and in the name of an unidentified and unmeasured "requirement of the public [fol. 933] interest," the Examiners would transfer vast amounts of this revenue to the very numerous Official and Midwestern roads without knowing the amount, without determining the roads in the East and Midwest that need additional revenues to perform essential transportation service, and without regard to the insignificant effect that any transfer of transcontinental revenues could have on the overall financial condition of Official and Midwestern lines dependent for 95% and 85%, respectively, of their freight revenue on other traffic.

Never have the Commission and the Courts authorized a transfer of divisional revenues on a "revenue needs" basis under such circumstances. On the contrary, adoption of the Examiners' recommendations would represent a reversal of the Commission's administration of Section

15(6) of the Act. This is most dramatically shown in *New England Divisions*, 66 I.C.C. 196, affirmed 260 U.S. 184, the landmark case in applying the revenue needs test under the Act. The Commission's conclusions are summarized in the following paragraph (66 I.C.C. at 206):

> "An increase of this amount in the divisions received by complainants would manifestly be of *benefit to them far greater than the detriment to their western connections.* To illustrate this: If the railway operating income of complainants had been increased by $7,500,000 in the 12 months ended September 30, 1921, their deficit of 0.87 per cent on investment would have been converted to an income of 0.04 per cent; while if the railway operating income of the other lines in the eastern group had been decreased by a like amount, the result would have been only a reduction in the amount earned on investment from 2.85 per cent to 2.76 per cent. It further develops that if the divisions now received by complainants on this merchandise traffic were increased by 15 per cent, subject to the limitations hereinafter set forth, the result, as nearly as can be estimated, would be an increase in revenue of not exceeding $7,500,000" (emphasis added).

In ordering a 15% increase in the divisions of the New England lines, the Commission thus found the amount of revenues which its divisional order would transfer, found that such amount was necessary to eliminate the deficit of the New England roads and found that a transfer of such revenues would not appreciably affect the revenues of their western connections (i.e., roads west of the Hudson River).

Contrast the Examiners' action here. No finding is made [fol. 934] as to the amount of funds which would be transferred by the recommended divisions. No finding is made as to the necessity of the transfer of any amount to the Official or the Midwestern roads. And no finding is made as to the effect on the Mountain-Pacific roads.

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[fol. 935]

Exception No. 7—To the Further Erroneous Statements in the Examiners' Recommended Report.

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[fol. 936] We have stated our position that the Commission should decide this case in the record before it and not enter upon a meaningless excursion into the passenger deficit issues. But if, nevertheless, the Commission is to consider passenger deficit issues, it can do so only after hearing on the new issues thus created (pages 23-24, *supra*). At any such hearing, we offer to prove that the rates of return for freight service, even using the unrealistic statistical passenger separation as the basis, produce the following comparisons:

	Rates of Return-Freight Service			
	1955	1956	1957	1955-1957 Average
Eastern District plus Pocahontas	6.02%	5.92%	5.10%	5.68%
Western District	5.99%	5.69%	5.29%	5.66%
Principal Transcontinental Lines	*	5.95%	*	*

* Not available, because the Rail Form A applications used in separating the property base as between freight and passenger are not available for the transcontinental lines except for the years of the cost studies of record.

These comparisons fail to reveal any "still greater degree of financial superiority for the western lines" as the Examiners speculate (sheet 31).

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[fol. 937]

Exception No. 8—To Certain Features of the Mechanics of the Group Basis of Divisions Recommended by the Examiners, Including Their Use of a 15% Minimum.

The divisions recommended by the Examiners are in the form of group percents, set forth in Appendix B to the recommended report. Our primary exceptions are not directed to the mechanics of the group basis of divisions, but to the unduly low level of the ("TC") percentages and the extreme revenue reductions which they impose on the Mountain-Pacific ("TC'") lines. For the reasons previously discussed in these exceptions, the percentages shown for the Mountain-Pacific lines should be increased substantially and those for the Midwestern and Eastern lines reduced correspondingly.

In recommending the group basis of divisions, the Examiners state that they agree "in general" with our position that "the present group basis of publishing transcontinental divisions is highly desirable in light of the competitive conditions affecting the routing of transcontinental traffic" (sheets 35-36). The Examiners have, however, as suggested by their qualification "in general", introduced changes in the present divisional basis and the mechanics and form of the group divisions recommended in their Appendix B raise numerous questions. For example, there is considerable uncertainty as to the precise outlines of geographical groupings, breaking points, definitions of the railroads to which the percents apply and other substantial questions. The extent to which the form of the recommended group basis of divisions would produce inequality and discrimination as between routes and carriers in violation of Sections 1(4) and 15(6) of the Act, and would destroy the parity of divisions that has existed through the years as a matter of competitive necessity, cannot be determined until these questions and ambiguities are resolved. It is premature to deal with these questions at this stage, however, because the

Examiners have themselves recognized the existence of many such questions and have provided that questions of divisions application be left to negotiations between the parties prior to the effective date of any order (sheets 36-38). Accordingly, we preserve our exceptions to these features of divisional mechanics until it is determined, in light of the possible resolution of the ambiguities and difficulties in the contemplated negotiations, what, if any, objections to the mechanics of the divisional basis then remain.

[fol. 938] However, it is appropriate at this time to take exception to one aspect of the divisions mechanics proposed by the Eastern and Midwestern roads—the proposed 15 percent minimum—which was accepted in part by the Examiners and which directly influenced the percents recommended for important categories of traffic. The Examiners rejected in terms the proposal of the Midwestern lines that "primary intermediate divisions should be subject to a 15-percent minimum" (sheet 35). But, without any discussion whatever, the percents recommended by the Examiners reflect a 15 percent minimum for origin or destination service. Thus the divisions from "South-Eastern Illinois" via any gateway, Chicago, Peoria or St. Louis, to the Pacific Coast are 15 percent (Appx. B, p. 18). Similarly, on Midwest-transcontinental traffic, the divisions recommended for the origin or destination lines are never less than 15 percent no matter how short the haul (Appx. B, p. 23).

On transcontinental traffic, with a total haul of over 2000 miles, on what basis can a group of roads with a 100 mile average haul be given 15 percent of the revenue? The average haul from the "South-Eastern Illinois" group is approximately 100 miles, since the most distant hauls from Vincennes and Evansville, Indiana, to St. Louis are only 150-170 miles. Nevertheless, under the Examiners' use of a 15% minimum, a line serving "South-Eastern Illinois" that performs only 100 miles of the total service, which is only 5% of the total haul, receives 15 percent of the total

revenue. Since terminal service could not justify an allowance equal to more than 100 miles under any cost basis (Exhibit T-653, p. 14), a division of 10% for the "South-Eastern Illinois" group would be excessive on the basis of any evidence in this record. The present divisions to the "South-Eastern Illinois" area range from 6 to 12 percent, depending upon the gateway (Exhibit E-1, p. 14). The Examiners would practically double the divisions of the "South-Eastern Illinois" lines through their use of a 15% minimum.

There is no basis in evidence, logic or precedent for the application of a 15 percent minimum to the short haul participant in the extremely long haul transcontinental traffic.* The Examiners' use of 15 percent as a minimum division in their recommended report is without justification, and no findings even purporting to justify the use of this, or for that matter any other, specific percentage are to be found in the Examiners' report.

[fol. 939] Conclusion

* * * * * * *

On the basis of the evidence of record, as contrasted with the fiction which underlies the recommendations of the Examiners, the Commission should make the findings which we have requested** and revise the divisions so as to increase, not reduce, the revenues of the Mountain-Pacific lines.

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* As discussed at pages 283-289 of the Brief of the Mountain-Pacific lines.

** As set forth in full under the heading "Requested Findings" in the Appendix to the Brief of the Mountain-Pacific lines.

[fol. 940]
Appendix II

APPENDIX II

The Issues Which Would Be Raised by Any Consideration of the Examiners' Charge of Excessive Passenger Deficits on the Transcontinental Lines.

As stated in our Exception No. 1, *supra,* the Examiners' charge that the transcontinental lines have "excessive passenger deficits." The Examiners base their recommended report on their creation of some $60 million in funds on the theory of a reduction of passenger deficits of the transcontinental lines in the same degree as the reduction in the statistical passenger deficits of the Official lines since 1948. In reaching these conclusions, the Examiners have made a series of underlying assumptions, all without any hearing, including the following:

1. That the returns from passenger operations in the East since 1948, a selected base year, constitute a reliable gauge and measure of efficiency in the conduct of the passenger operations of the transcontinental lines;

2. That the passenger traffic, facilities, service and operations in the East, in 1948 and thereafter, were comparable to the passenger business in the territory served by the transcontinental lines;

3. That the extensive passenger train discontinuances inherent in the Examiners' conclusions would be approved by the States or by this Commission, without reference to the specific facts of record in the individual proceedings and the consideration by these tribunals of the public need for the service;

4. That such train discontinuances would produce, not merely reductions in a statistical deficit, but actual dollar savings of $60 million or more annually; and,

5. That the potential for future dollar savings is greater for the "transcontinental lines" than for the Official lines.

In this Appendix we shall show, as to each of these assumptions, the errors made by the Examiners in light of evidence which we offer to prove in the hearing concerning this new charge which will be necessary if the Commission decides to consider this new subject instead of properly deciding this divisions case on the comprehensive record made by the parties.

[fol. 941] The following summary treats with each of the Examiners' underlying assumptions in the order listed above.

1. The return from passenger business in the East since 1948 do not constitute a reliable gauge or measure of efficiency in the conduct of the passenger operations of the transcontinental lines.

The sole reason given by the Examiners for the selection of 1948 is that (sheet 27):

> "The use of 1948 as a base is appropriate because in that year the total passenger deficit of all railroads reached half a billion dollars for the first time in railroad history"

This provides no sensible reason for selecting 1948 as a base in comparing the experience of Eastern and other roads. The cause of the total passenger deficit reaching half a billion dollars in 1948 could well be that the Eastern roads had let their passenger losses get out of control in the immediate post-war period. The Examiners would then be selecting a base year for the very reason that disqualifies the year as a proper base, since the Eastern lines' deficits were abnormally high relative to those of other roads in 1948.

This is the fact, as may be shown by using the Examiners' own approach (sheet 28), but substituting pre-World War II experience as the base and testing the passenger deficits in 1948:

Passenger Deficits (Thousands)

Year	Eastern District and Pocahontas Region	Western District	Transcontinental Lines (AT&SF, D&RGW, GN, NP, SP, UP)
1939	$ 93,311	$125,230	$ 51,731
1948	252,145	234,625	107,492
Percentage change, 1939 to 1948	+170%	+87%	+108%

Paraphrasing the Examiners' conclusions (on sheet 28) to apply to the 1939 to 1948 changes in passenger deficits:

> If the rail carriers in Official territory had been able to hold their average annual passenger deficit in 1948 to a figure only 87 percent more than their 1939 deficit, as did the Western lines, their revenue saving would have been nearly $78 million per year. The annual [fol. 942] saving of the Official lines relative to the experience of the transcontinental lines similarly estimated would have been more than $58 million annually.*

Thus, the Examiners' own approach would establish the year 1948 as one of "excessive passenger deficits" for the Official roads.

Furthermore, the Examiners' approach, if injected by them into the recent *Official-Southwestern* and *Official-Southern* Divisions cases in which they also sat, would have impeached the result which the Commission reached in

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*Substantially the same results are produced by the use of any of the pre-war years, 1936, 1937, 1938 or 1939.

those cases (287 I.C.C. 497 and 553). The following table compares the passenger deficit experience of the roads there involved:

Passenger Deficits (Thousands)

Year	Eastern District and Pocahontas Region	Southwestern Region	Southern Region
1939	$ 93,311	$25,949	$32,393
1948	252,145	$45,013	$72,982
Percentage Change 1939 to 1948	+170%	+73%	+125%

Again paraphrasing the Examiners' conclusions (sheet 28) to apply to the 1939 to 1948 change in the passenger deficits of these groups:

> If the rail carriers in Official territory had been able to hold their average annual passenger deficit in 1948 to a figure only 73 percent more than their 1939 deficit, as did the Southwestern lines, their revenue saving would have been nearly $91 million per year. The annual saving of the Official lines relative to the experience of the Southern lines similarly estimated would have been more than $42 million annually.

Again the Examiners' approach would establish the year 1948 as one of "excessive passenger deficits" for the Official roads. Thus, the Examiners' failure to inject this issue into the *Official-Southwestern and Official-Southern* cases would, under their present theory, impeach the result reached by the Commission in its decisions in those cases. [fol. 943] In further support of the showing that the year 1948 does not provide a proper benchmark for comparing changes in passenger deficits of Eastern roads, we offer to prove that, in 1948 and preceding years, the Mountain-Pacific lines have been diligent in studying the revenue

experience of individual passenger trains in light of their costs of operation and in undertaking to act promptly in seeking discontinuance of trains not covering their out-of-pocket costs. Inquiry would also be required into the degree of activity of the Eastern and Midwestern lines as to whether they also had been aggressive in studying and discontinuing such unprofitable trains.

2. The passenger traffic, facilities, service and operations in the East in 1948 and today are not at all comparable with the passenger business in the territory served by the Mountain-Pacific lines.

The Examiners' conclusions as to "excessive passenger deficits" on the Mountain-Pacific lines, based solely on comparison with changes in statistical passenger deficits of Eastern lines since 1948, disregard entirely the vast differences in conditions confronted in the respective territories.

The Examiners' underlying assumption that the Mountain-Pacific lines have been inefficient and dilatory in discontinuing unpatronized passenger train service takes no account of the differences in the passenger traffic and service in the different territories. Analysis of the facts as to passenger traffic and reduction of train service in the respective territories, however, completely refutes the Examiners' conclusions. The following table shows the changes in passenger traffic since 1948:

Revenue Passenger Miles—Millions

Year	Eastern District and Pocahontas Region	Western District	Transcontinental Lines (AT&SF, D&RGW, GN, NP, SP, UP)
1948	21,505	14,209	7,293
Average 1949-1959	14,519	11,146	5,944
Percent Change	—32%	—22%	—18%

In light of this decline in passenger traffic, all roads have [fol. 944] reduced their passenger train service, but in differing proportions, as shown in the following table:

Passenger Train Miles—Millions

Year	Eastern District and Pocahontas Region	Western District	Transcontinental Lines, (AT&SF, D&RGW, GN, NP, SP, UP)
1948	179	169	75
Average 1949-1959	130	136	63
Percent Change	—27%	—20%	—16%

As shown, the Western District and Transcontinental lines have reduced passenger train service in proportion to the reduction in passenger traffic (20% vs. 22% in Western District, and 16% vs. 18% on the transcontinental lines). The Eastern lines have not shown any better performance but have lagged behind, reducing passenger service by only 27% with a decline in passenger traffic of 32%.

Another outstanding difference between the passenger operations of the Eastern and other groups of roads is the frequency of passenger trains which each group operated in 1948, the base year selected by the Examiners. The following table compares the daily frequency of passenger trains:

	Passenger Train Miles per day per Mile of Road in each Direction (year 1948)
Eastern District plus Pocahontas Region	6.1
Western District	2.6
Transcontinental lines (AT&SF, D&RGW, GN, NP, SP, UP)	3.1

As shown, the East had twice the Western lines' frequency of passenger trains in 1948. Obviously, the opportunity for discontinuances of train service were greater for the Eastern lines. The chance of success in an attempted discontinuance of one of six pairs of trains per day is far greater than in the attempted discontinuance of the last pair of trains over a given line.

Moreover, in areas such as the East and parts of the Midwest where several different roads serve the same com- [fol. 945] munities, it is much more likely that the entire discontinuance of passenger service by a railroad would be permitted when one or more of the other roads continues to provide rail service. For example, the B&O discontinued service between Washington and New York while the PRR discontinued trains between Washington and Chicago. In Mountain-Pacific territory, however, there are many important points serving vast areas which are connected by only one railroad. (Salt Lake City and Los Angeles by the UP, Great Falls and Seattle by the GN, and many others.)* With passenger service between many such points now at a bare minimum, further discontinuances would result in entire elimination of rail passenger, mail, and express services in large areas. This is vastly unlike discontinuances of service in the East and Midwest where rail passenger service is still available over another road.

Another marked difference between the passenger business in Official and Western territories is the existence of important passenger runs which contribute substantially above their out-of-pocket costs. The Washington-New York run on the Pennsylvania is an example. The existence of such high density profitable runs, when averaged with the other passenger services in the East, obscures the Official lines' performance in dealing with unprofitable pas-

* In an instance where several roads serve the same points (NP, GN and UP between Seattle and Portland), passenger service had been pooled for many years prior to 1948. See *Puget Sound-Portland Joint Passenger Service*, 96 I.C.C. 116.

senger service. This deprives of any meaning statistical comparisons with roads operating in Mountain-Pacific territory where there are no offsetting instances of relatively profitable high density passenger traffic.

A further significant difference in the passenger business in the East is the high proportion of facilities solely related to passenger service. This includes not only extensive commuter lines but also additional intercity tracks constructed and maintained solely for passenger service. On the other hand, a great deal of the mileage of the Mountain-Pacific roads must be maintained in any event for freight service. One consequence of this difference is that the New York Central was able to obtain large savings through the elimination in 1957 of the two passenger tracks of the former four-track line between Cleveland and Buffalo, for example (Exhibit T-339, p. 9). No opportunity [fol. 946] for such savings exists on the Mountain-Pacific roads whose single or double track lines must be maintained for freight service.*

The difference in the character of the passenger facilities in the respective territories is reflected in the fact that the percentage of costs allocated to passenger service which would be avoided if passenger service were discontinued has been determined to be substantially greater in the East than in the West. Indeed, the officer of the New Haven who presented a study of "the approximate long term avoidable cost of passenger service of the railroads of this country treated as a whole" referred to in *Railroad Passenger Train Deficit*, 306 I.C.C. 417, 424, used a single figure as the percentage of passenger expenses which were

* The situation of the Mountain-Pacific lines is comparable to that described by the Supreme Court in *King* v. *United States*, 344 U.S. 254, 265:

> "In Florida, moreover, the discontinuance of railroad passenger service would not permit the discontinuance of high speed tracks and equipment because of the need for fast freight schedules to transport perishable fruits and vegetables from Florida."

avoidable on a national basis, but he constructed this figure by using a different and substantially lower percentage for the Western roads than for the Official roads.*

3. Passenger service cannot be discontinued without regard to the standards of approval established by the state agencies or by this Commission.

The Examiners' admonish the Mountain-Pacific state commissions to take "a sympathetic attitude toward discontinuance of unprofitable passenger service" (sheet 31). The Examiners' admonition, as well as their conclusions, assume a radical change in the approach of all regulatory agencies concerned with passenger service, including this Commission.

In train discontinuance proceedings, one of the prime factors considered and determined is the "public need" for the rail passenger service. The determination of "public need" is necessarily concerned with the specific facts of record in the individual proceedings. The policies of state regulatory bodies may vary in the determination of "public need", but certainly this Commission cannot presume a policy for state regulatory agencies less stringent [fol. 947] than the approach which this Commission itself applies in administering train discontinuance cases under the 1958 Amendment to Section 13 of the Act (49 U.S.C. § 13a (1). The Commission** has, in some cases, refused to permit the discontinuance of passenger trains operating at out-of-pocket losses on the ground that continued operation was "required by the public convenience and necessity".*** Moreover, the Commission takes into account not

* Docket 31954, V.S. No. 94, p. 41.

** In citing train discontinuance cases under Section 13a(1), references to decisions by the Commission refer to decisions by the appropriate Division of the Commission, formerly Division 4.

*** Louisville & N.R. Co. Discontinuance of Service, Ocean Springs, Miss.-New Orleans, La., 307 I.C.C. 173; Louisville & N.R. Co. Discontinuance of Service, Bowling Green, Ky.-Memphis, Tenn.,

only the revenues collected for the particular train as to which discontinuance is sought, but also considers the "feeder value" of its passengers, mail and express to other passenger trains.[8]

The Examiners disregard the interpretation and corresponding weighing of public need by the State tribunals and by this Commission and, in effect, the Examiners prejudge an extensive series of train discontinuance cases when they presume the creation of over $60 million in additional funds for the transcontinental lines annually through extensive train discontinuances (sheet 31).

4. Most significantly, the Examiners err in assuming that train discontinuances could produce $60 million in actual dollar savings to the Transcontinental Lines.

In presuming that extensive train discontinuances will produce savings of $60 million for the Mountain-Pacific lines, the Examiners disregard the Commission's own consistent line of decisions in train discontinuance cases under Section 13a(1) of the Act. In such cases, the Commission requires evidence showing the dollar savings which would result from discontinuance of a train. The expenses which are recognized in these determinations differ greatly from the passenger expenses which enter into the calculation of the statistical passenger deficit.

[fol. 948] For example, the statistical passenger deficits relied upon by the Examiners include expenses for maintenance-of-way and structures allocated to passenger service. As the Commission stated in *Railroad Passenger Train Deficit*, 306 I.C.C. 417, 420:

"The criticism of our separation rules is based on the fact that only about 75 percent of the passenger

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307 I.C.C. 392. See also Southern Pacific Co., Change of Passenger Service Between Oakland, Calif. and Ogden, Utah, ... I.C.C. .... (decision dated January 26, 1961, Finance Docket 21255).

[8] Louisville & N.R. Co., Discontinuance of Service, Bowling Green, Ky.-Memphis, Tenn., 307 I.C.C. 392, 399.

operating expenses as reported can be directly separated from those for freight service. These are known as solely related expenses. Obvious examples are wages of trainmen and enginemen in passenger operation. The other 25 percent, which are not solely related, present a typical problem in the ascertainment of the components of common costs. For the most part, the costs which must be apportioned are in the group of accounts for maintenance of way and structures."

Whatever the merits of the controversies as to the treatment of common passenger expense, the fact is that the Commission does not use in its train discontinuance cases the statistical apportionment which enters into the computation of the statistical passenger deficit. Instead, the Commission assumes that the maintenance of way and structures expenses allocated to passenger service must be incurred in any event whether or not the passenger service is continued. Ties deteriorate and must be replaced, bridges must be painted, and many of the other expenses statistically assigned to passenger service must be incurred in any event as part of the freight service.

Thus, the Commission, acting on the basis of this theory in its train discontinuance cases, excludes entirely the maintenance of way and structures expenses in determining the out-of-pocket costs of trains sought to be discontinued.* The Commission also excludes joint facility expense,** traffic and general overhead expenses,*** station

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* Atchison, T.&S. F. Ry. Co. Discontinuance of Service Between Kansas City, Mo. and Houston, Tex., 312 I.C.C. 79, 84-85; Louisville & N.R. Co. Discontinuance of Service, Ocean Springs, Miss.-New Orleans, La., 307 I.C.C. 173, 180; Louisville & N.R. Co. Discontinuance of Service, Bowling Green, Ky.-Memphis, Tenn., 307 I.C.C. 392, 398.

** Atchison, T.&S. F. Ry. Co. Discontinuance of Service Between Kansas City, Mo. and Houston, Tex., 312 I.C.C. 79, 85; Louisville & N.R. Co. Discontinuance of Service, Ocean Springs, Miss.-New Orleans, La., 307 I.C.C. 173, 180-182; Louisville & N.R. Co. Discontinuance of Service, Bowling Green, Ky.-Memphis, Tenn., 307 I.C.C. 392, 398.

*** Southern Pacific Co. Partial Discontinuance of Passenger Service, San Francisco, Calif.-Portland, Ore., 307 I.C.C. 209, 217;

[fol. 949] and terminal expenses,* snow removal** and hauling company material*** in determining the dollar savings which would be realized by train discontinuances.

The Commission's train discontinuance cases thus define the elements of expense which the Commission includes in determining annual dollar savings. The Commission's action in these cases is given emphasis in the *Passenger Train Deficit* case in which it is stated that the statistically apportioned passenger expenses, relied upon by the Examiners, "do not reflect, nor are they intended to provide, the cost of operating individual trains; they are not intended to determine the expenses which would be avoided if all passenger services were discontinued; and they are not intended to measure the elusive 'out-of-pocket' costs." 306 I.C.C. at 427.

The extent of the difference between the statistical deficits upon which the Examiners rely and the costs which are taken into account by the Commission as indicating actual dollar savings in train discontinuance cases is very great. For example, the statistical deficit apportioned to the trains at issue in one recent case totalled $1,000,000, but the Commission found that the annual savings resulting from discontinuance would be only $225,000.**** It is thus appar-

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Chicago & N.W. Ry. Co. Discontinuance of Service Between Chicago, Ill. and Duluth, Minn. and Mankato, Minn., 307 I.C.C. 585, 607; Texas & N.O.R. Co. Discontinuance of Service Between Houston, Tex. and New Orleans, La., 307 I.C.C. 725, 731.

* Southern Pacific Co. Partial Discontinuance of Passenger Service, San Francisco, Calif.-Portland, Ore., 307 I.C.C. 309, 217; Chicago & N.W. Ry. Co. Discontinuance of Service Between Chicago, Ill., and Minneapolis, Minn., 307 I.C.C. 271, 280-281.

** Chicago, M. & St. P. R.R. Co., Discontinuance of Service Between Madison, Wis. and Canton, S. Dak., 307 I.C.C. 565, 578.

*** Texas & N.O.R. Co. Discontinuance of Service Between Houston, Tex. and New Orleans, La., 307 I.C.C. 725, 731.

**** Chicago & N.W. Ry. Co., Discontinuance of Service Between Chicago, Ill. and Minneapolis, Minn., 307 I.C.C. 271, 280-281.

ent that a passenger train operating at a loss as reflected in the statistical passenger deficit may actually produce revenues in excess of the costs which the Commission will recognize in computing annual savings in train discontinuance cases.

[fol. 950] The following table illustrates the extreme difference between the costs which the Commission includes in determining annual dollar savings in train discontinuance cases and the statistically apportioned expenses which enter into the statistical passenger deficits relied upon by the Examiners:

	Transcontinental Lines (AT&SF, D&RGW, GN, NP, SP, UP) (Year 1959) (000)
1. Total Passenger Train Revenues	$232,215
2. Total Passenger Expenses in Accounts Considered by Commission in Train Discontinuance Cases	$206,039
3. Contribution of Revenues in Excess of Expenses Allowed in Train Discontinuance Cases (line 2 minus line 3)	+$ 26,176
4. Total Passenger Revenues	$237,476
5. Total Expenses Statistically Apportioned to Passenger Service in Annual Reports	$396,665
6. Statistical Passenger Deficit (line 4 minus line 5)	—$159,189

As shown in this table, the statistical passenger deficit reflects total expenses, including apportioned expenses, of $396,665,000 for the transcontinental lines. In contrast, the expenses in the accounts which the Commission includes in its consideration of train discontinuance cases total only

$206,039,000. This difference of nearly $190 million is due almost entirely* to the difference between the Commission's approach in train discontinuance cases, where it is calculating annual dollar savings, and the very different calculation of the statistical passenger deficit which reflects all expenses allocable to passenger service, whether or not the expenses would be saved by discontinuance of particular trains.

The Examiners, nevertheless, equate train discontinuances with annual savings to our roads without recognizing that a reduction in the statistical passenger deficit through the discontinuance of a train does not produce a saving in dollars equal to the statistical deficit, but transfers some [fol. 951] portion of the apportioned costs to the freight service which must bear those costs in any event. Indeed, trains which produce revenues in excess of their actual out-of-pocket costs, properly determined, but less than the apportioned passenger expenses, would, if discontinued, reduce the statistical deficit but cast the apportioned costs against freight service while losing a contribution above out-of-pocket costs.**

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* As shown by the fact that the total passenger train revenues of the transcontinental lines ($232,215,000) account for substantially all of the total passenger revenues ($237,476,000).

** This was explained by James M. Symes of the Pennsylvania as follows (Exhibit T-337, p. 87):

"Q. What is this formula?

A. The ICC has a formula that allocates costs, that is, passenger service standing a certain percentage of the track used for both freight and passenger, overhead, and so forth, which they call the "full-cost-formula"—with which I find no fault, because something's got to carry these costs.

And on that basis the industry lost about 700 million dollars last year. We on the Pennsylvania alone lost 49 million. Of course, on an out-of-pocket cost basis we lost only a fraction of that.

Q. Well, those so-called "full costs" do not include cost of the roadbed, do they?

A. They include the cost of maintaining the roadbed.

Q. Wouldn't you have to maintain the roadbed for freight, anyway?

A. That's right, you would have to have a great part of it. Here is the irony of the passenger situation as an example: On

The significant fact is that the statistical passenger deficits, used by the Examiners as their sole basis for creating the $60 million of additional funds upon which they predicate their decision, are unreal in the sense that they include expenses which cannot be discontinued but which must be incurred in any event for freight service. The Examiners lose all touch with reality in presuming that train discontinuances can produce $60 million annually for our lines in actual savings to be used to absorb reduced transcontinental divisions or for any other purpose.

5. If there is any potential for savings, it is no greater on the Transcontinental roads than on the Eastern or Midwestern roads.

Inherent in the Examiners' comparison of passenger defi- [fol. 952] cits and finding of "excessive passenger deficits" on our roads is the assumption that the "potential source of increased revenue" is greatest on the transcontinental lines and least on the Eastern lines (sheets 30-32). This conclusion is demonstrably erroneous. On the contrary, the Eastern lines appear to have a potential for obtaining actual savings beyond that of the transcontinental lines. As documented in the legislative history of the Transportation Act of 1958, it was the Eastern state commissions, particularly New York, New Jersey and Pennsylvania, that were least "sympathetic" to carriers' efforts to remove passenger service operated at an out-of-pocket deficit.*

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a full-cost basis we should get about $8 a train-mile in revenue. We are actually getting about $6, so we are losing nearly $2 a train-mile—pretty close to it. But if we take that train off, we actually save around only $4 a train-mile.

We have the investment of nearly a billion dollars in our passenger facilities. We have the roadway, as you say. So that we find ourselves in the position that we can't afford to take off a passenger train-mile that is producing $6 even though the full cost is $8, knowing that we're only going to save $3.50 or $4."

* Hearings before House Committee on Interstate and Foreign Commerce on "Railroad Problems", 85th Cong., 2d Sess., pp. 224-

Furthermore, the Eastern lines are at the threshold of obtaining contribution for the facilities solely related to commuter service. The Commission recently recommended, *Railroad Passenger Train Deficit*, 306 I.C.C. 417, 483:

> "That where the railroads are unable to operate a particular local or commuting service, and where such service is essential to the community or communities served, that steps be taken by State and local authorities, or both, to provide the service paying the carrier the cost plus a reasonable profit."

The Eastern railroads, acting on this sound approach, are now receiving some $6 million annually from the State of New Jersey, and are in the process of obtaining direct support of commuter operations or tax relief in New York, Connecticut and Pennsylvania. None of this potential for actual dollar savings in tax expenses or contributions to revenue is reflected in the Examiners' statistics or taken into consideration in assuming that our roads have a far greater potential for annual savings from their passenger operations.

As to passenger traffic other than commuter service, the outlook for the short haul passenger service in the East is much brighter than for the transcontinental passenger hauls. As Mr. Symes of the Pennsylvania has stated (Exhibit T-337, p. 51):

> [fol. 953] "Realistically, we do not see much future for rail transportation in extremely long passenger hauls where the time element is so much of a factor. By the same token, we believe there is a favorable future for rail transportation in passenger hauls between metropolitan areas involving distances of one hundred to a thousand miles. The Pennsylvania Rail-

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225, 299-300. Hearings before Senate Committee on Interstate and Foreign Commerce, "Problems of the Railroads", 85th Cong., 2d Sess., pp. 230-231.

road is well situated to serve this potential mass travel market between large cities.*

This shows that there is no basis whatever for the Examiners' conclusion, based solely on statistical passenger deficits, that our lines have a potential for savings in passenger service exceeding that of the Eastern lines.

For the foregoing reasons, each of the assumptions made by the Examiners in relying upon statistical passenger deficits is seriously in error. We offer to prove the facts set forth above in respect to the charge of "excessive passenger deficits," made by the Examiners on the basis of data outside the record and without any hearing, if the Commission decides to pursue this charge instead of deciding this divisions case on the record made by the parties.

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* Mr. Symes repeated this position in 1958 before the House Committee on Interstate and Foreign Commerce, "Railroad Problems," 85th Cong., 2d Sess., p. 303:

> "As to our dense passenger service operating between New York, Philadelphia, Baltimore and Washington, the potential here is tremendous. Even with the improved highways skirting congested areas and with tunnels and bridges shortening distances, the parking problem is a major difficulty in every metropolitan area. Additionally, the time saving by air in this territory is not too much of a handicap. So our answer in this densely populated area seems to be frequent service on symmetrical schedules at low fares, which could very well preserve the operation of this service at a profit for many years to come."

[fol. 954]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

TRANSCONTINENTAL DIVISIONS CASES

Docket No. 31503

(and Sub-Nos. 1-5)

THE AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY, et al., Complainants,

vs.

THE ATCHISON, TOPEKA AND SANTA FE RAILWAY COMPANY, et al., Defendants.

Exceptions of the People of the State of California and the Public Utilities Commission of Said State to Recommended Report

William M. Bennett, Cyril M. Saroyan, Attorneys for the People of the State of California and the Public Utilities Commission of said State, 514 State Building, San Francisco 2, California.

(Due Date: April 5, 1961)

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[fol. 955]

III.

Revenue Needs

Exception No. 5

In discussing the matter of revenue needs, the recommended report commences once again with a reference to the report in *Class Rates, Mountain-Pacific Territory, supra,* by saying at page 20 that the Mountain-Pacific States Commissions "were there supporting a reduction in

the class rates but are here aligned with the defendants in [fol. 956] arguing for an increase in their divisions."

Argument on Exception No. 5

The quoted statement is not only gratuitous, but erroneous. It misstates the position of most of the State Commissions in the class rate case, and misstates the position at least of the California Public Utilities Commission, an intervener, in the instant case. On the latter point, we need only repeat the following language from page 9 of the brief filed by this intervener in the instant cases:

> "In view of the language of Section 15(6) of the Act, however, it is urged that the Commission give due consideration to the tremendous importance to the public of the transportation services of the rail carriers. The People of the State of California, and their economy, are dependent upon the transcontinental railroads. If the railroads terminating in California should be deprived of earnings by reductions in divisions, their ability to serve the People of this State adequately, and at reasonable rates, would be seriously impaired."

Exception No. 6

Under the subject of revenue needs, the recommended report undertakes first to show that the Mountain-Pacific Territory has expanded more rapidly in terms of economic development in recent years than has the Eastern District, and that the transcontinental railroads have advanced proportionately more than the eastern railroads in the terms of tonnage, freight revenue and net railway operating income (pages 20, 21 and 22 of the recommended report).

[fol. 957] Argument on Exception No. 6

These statements are misleading and deceptive. Whatever significance may be attached to the selected figures

expressed on those pages, the Examiners have not related them to any finding or conclusion. If the transcontinental lines have grown in importance (page 22), their revenue needs may be greater, not less. Do the Examiners wish to infer that the divisions have produced the tonnage? Speculate as we will, the Examiners have not left any clue from which we can determine what they think to be so significant in the "growing importance of the transcontinental lines" or in "the inferior position of the railroads in official territory as freight carriers" (page 22), or in any of the similar matters referred to on pages 20, 21 and 22 of the report. If economic growth produces more tonnage, which produces more revenue, which, in turn, results in more income (accompanied by more expenses), what is the bearing upon revenue needs or equitable divisions of revenue between carriers? Increasing tonnages may produce more revenues, more expenses, and more income, and in the end the revenue *need* may be greater than before. If divisions of revenue are to be adjusted because of some consideration of revenue needs, it is essential that the revenue needs be clearly comprehended and determined.

Exception No. 7

In their consideration of comparative rates of return on investment, the issue of returns measured by book invest- [fol. 958] ment base or "elements of value" base is discussed (pages 22-25). The recommended report states as follows at page 25:

> "In our judgment, controlling weight should be given the showing based on elements of value consistently with the views expressed by the Commission in other divisions cases."

Argument on Exception No. 7

This conclusion is not warranted. No reason is given for the conclusion embraced other than certain references to

other proceedings, in one of which "the Commission was not impressed" (page 24) and in the other of which "the then director of the Commission's Bureau of Accounts & Cost Finding proposed an accounting order", which recommendation was not acted upon (page 25).

These reasons and impressions are very unsubstantial ones upon which to draw a conclusion that controlling weight should be given to the rate base advocated by the railroads of the Eastern District and opposed by the railroads of the transcontinental group.

IV.

Revenue Needs—Operating Efficiency

Exception No. 8

In continuing their discussion relative to the consideration of revenue needs, the Examiners (page 25 and following) turn to the subject of relative operating efficiencies after saying "but in the nature of things such consideration [fol. 959] presents great difficulty in assigning a definite weight to this element in appraising either cost or revenue need."

Referring to the Eastern District railroads, the Examiners say: "Even if it be conceded that there may have been some inefficiency in their past operations, that circumstance would not bar the possibility that insufficient freight revenue, due in part to inadequate divisions, was to some extent a contributing cause." (page 26)

Argument on Exception No. 8

The above statement is argumentative! What are the actual facts? They are not disclosed. It might be argued just as convincingly that any apparent insufficiency in past freight revenue is attributable to operating inefficiencies.

The Commission is required to give "due consideration, among other things, to the efficiency with which the carriers concerned are operated", and it is not enough for the Ex-

aminers to say that such consideration presents great difficulty and to argue concerning the possibilities that may exist. A more profound understanding and analysis of the evidence is necessary, and findings of fact are required. *Lawful and proper disposition of these proceedings requires not argument from the Examiners, but findings of fact upon which conclusions may be predicated.*

Exception No. 9

At page 27 of the recommended report we find the following language: "Contrary to popular impression, however, [fol. 960] in this period [the past ten years] the passenger deficit has been larger in the West than in the East, and the eastern carriers have done better in reducing their passenger deficits than the western lines." The report states as follows, at page 31:

> "It has already been pointed out in this report that the various changes in the country's freight-rate structure in the past 15 years have not prevented the mountain-Pacific railroads from attaining a greater degree of prosperity as freight carriers than the eastern and midwestern lines. The mountain-Pacific lines, however, are losing relatively much more money than the others on their passenger traffic, and we see no reason for offsetting those losses by increases in their revenue from transcontinental freight. The obvious answer to the question stated in the foregoing quotation* is that a reduction in the passenger deficit of the mountain-Pacific lines, which would seem to be imperative sooner or later, should help materially in furnishing funds for

* Referring to the question cited in a quotation from an intervener's brief which asks "Where then is the money necessary to provide additional facilities, and to maintain the earnings of the Mountain-Pacific carriers to come from?" [in order that they be able to obtain necessary funds to increase facilities to keep pace with the expanding economy of the Mountain-Pacific States] (pages 30-31 of recommended report).

additions and betterments. The interveners are in a position to assist in such a course by taking a sympathetic attitude toward discontinuance of unprofitable passenger service. The American railroads other than the defendants in 1959 had a total passenger deficit 15 percent lower than they had in 1948. If the defendants had been able to do as well, they would have had a saving of $67.8 million in 1959."

Argument on Exception No. 9

The above statements and several others contained within pages 27 through 31 of the recommended report draw a [fol. 961] conclusion which rests on a false premise. The report undertakes to show that the eastern lines have been more successful in reducing passenger deficits than have the transcontinental lines. It thereupon draws the conclusion that the transcontinental lines may offset a reduction in freight divisions with a future reduction in passenger losses. This line of thinking, we submit, is patently ridiculous.

The Commission is required, in a divisions case, to give consideration to the revenue needs of the carriers. In such consideration, revenue needs cannot be nicely classified as freight revenue needs, passenger revenue needs, and other revenue needs. The railroads have a continuing need for revenues adequate to render *all* of their essential services to the public, and these services include the transportation of both freight and passengers as may be necessary. The Examiners should know that it avails nothing in a general freight rate increase proceeding to urge, against the increase, that passenger deficits should not be considered. It is well-established that all of the revenue needs of the carriers must be considered in a general nationwide freight rate case. How, then, can the Examiners suggest in a general nationwide case concerning the *divisions* of the freight revenues that passenger deficits need not be considered in determining the relative revenue needs of the carrier

groups? This reasoning of the Examiners is fallacious, and the predication of any conclusions upon such reasoning *is fundamental error.*

[fol. 962] The comparisons made between the passenger deficits and relative changes for the transcontinental and eastern railroads and the conclusions reached therefrom are not proper and are in error for the following further reasons:

1. No data or evidence is included in this record to support the comparisons and conclusions. This intervener presented to the Commission considerations relating to the need of the People of the State of California for expanded and modernized rail plant and facilities of the railroads serving this area so that they might be able to better serve the expanding economy of the area and for more adequate transportation to distant markets. The Examiners have paid very little attention to these considerations and have countered by bringing up the passenger deficits of the transcontinental railroads and chided both the railroads and the commissions in the western states for the existence or the size thereof. While some of the figures as to alleged passenger deficits as reported to the Commission may be in the record, there had been no issue made concerning this subject in the testimony or in the briefs. It is submitted that Examiner Hosmer evidently had fixed opinions concerning this as a result of the report he rendered in the *Railroad Passenger Train Deficit Case,* Docket 31954, and he took occasion to inject them into this case.

2. Even if it were proper for the Commission to take official notice of such data from their records, the compari-

[fol. 963] sons made and the conclusions reached are not proper and are in error because:

(a) There is no basis to show that at the starting point of 1948 the transcontinental and eastern railroads were on an even footing. In fact, they definitely were not. For example, the competitive situation between the transcontinental railroads for passenger traffic has

at no time been comparable to that of the eastern railroads. In the East, service between many points is provided by a number of different railroads while in the West, there are only a few points between which more than one railroad provides service. Also there is a far more extensive network of rail passenger service operated in the East than in the West, particularly since 1948, the beginning of the period used by the Examiners for comparisons. These conditions provide a much greater potential for reduction of passenger train service in the East than in the West, and in addition, require the state regulatory agencies in the western states to give much greater weight to the question of public convenience and necessity when considering the possibility of service discontinuance.

(b) The passenger deficits which are used as the basis of the comparisons and the resulting conclusions are based on full cost allocations and in no way reflect actual savings or "avoidable expenses" if the service [fol. 964] were discontinued. The Commission's decision of May 18, 1959, in Docket 31954 (Railroad Passenger Traffic Deficit), 306 I.C.C. 417, 427 (Advance Sheets), states in relation to reported passenger deficits "The separation rules . . . are not intended to determine the expenses which would be avoided if all passenger services were discontinued; and they are not intended to measure the elusive 'out-of-pocket' costs."

(c) To suggest that the transcontinental roads make further reductions in their present minimum level of passenger service presents a critical problem and is not consistent with the conclusion of the Commission stated in the above decision at page 484, which states that: "We are of the view that a complete elimination of passenger-train service would not be a solution in the public interest. Economic railroad passenger service is, and for the foreseeable future will be, an integral

part of our national transportation system and essential for the Nation's well-being and defense."

Exception No. 10

The Examiners state at page 31 that a reduction in the passenger deficit of the Mountain-Pacific lines should help materially in furnishing funds for additions and betterments, and that the "interveners are in a position to assist in such a course by taking a sympathetic attitude toward discontinuance of unprofitable passenger service."

[fol. 965] Argument on Exception No. 10

The Examiners should know that the transportation policy of the United States does not contemplate that all unprofitable services shall be arbitrarily discontinued. The record in this proceeding does not establish the relative amounts of sympathy displayed by the state commissions in various parts of the Nation in the discharge of their duties. The Examiners have gone afield in advising and admonishing the interveners concerning subjects which are not in issue in these proceedings and which obviously are beyond the knowledge or responsibility of the Examiners.

Furthermore, it is an encroachment upon the province of state commissions for the Examiners to undertake to judge what their determinations should be as to appropriate passenger services. It must be borne in mind that these matters, at least in so far as intrastate passenger service is concerned, are vested initially in the appropriate state bodies, under the specific procedures authorized by the Transportation Act of 1958.

V.

Conclusions of the Examiners

Exception No. 11

Starting at page 33 and ending at page 38, the Examiners set forth some four pages of conclusions. The first three

paragraphs under "Conclusions" appear to be intended to form the basis and support for all of the conclusions that [fol. 966] follow. The first paragraph states as follows:

> "The proposal of the defendants and their intervening allies that the divisions of those carriers be increased at least 10 percent ostensibly is premised on a contention that, as the transcontinental traffic accounts for some 50 percent of their revenue, that traffic should in large measure afford (1) satisfactory dividends to stockholders, (2) a depressed rate structure which would continue to give mountain-Pacific producers access to eastern markets, (3) funds for the financing of improved facilities necessary to serve the growing West, and (4) inferentially a passenger deficit amounting to nearly $160 million per year. To require an increase in their divisions to further these objectives seems to us so palpably unfair to the midwestern and eastern lines that we are inclined to regard the proposal as a defensive maneuver in the nature of a diversion (in the military sense of the word)." (page 33)

Argument on Exception No. 11

The Examiners have disclosed some prejudices and misconceptions in the above statement which, we believe, have led to erroneous conclusions. Without any preliminary findings of fact, they have simply dismissed out-of-hand the proposal of the defendants "and their intervening allies" (to whom do they refer?) as "palpably unfair".

Which of "these objectives" are so distasteful to the Examiners that they think it would be palpably unfair to further such objectives through an increase in the division of freight revenues? The Commission long has recognized, as it must, that investors should be compensated, that railroads must finance improved facilities largely from earnings, and that passenger services, though sometimes unprofitable, are a necessary function of the national trans-

[fol. 967] portation system. What do the Examiners mean by "a depressed rate structure which would continue to give mountain-Pacific producers access to eastern markets"? Would the Examiners have the railroads establish a rate structure under which the products of the West would *not* have access to the eastern markets? Would the national transportation policy be served by a rate structure under which the populous East would be deprived of the products of California, the principal agricultural state in the Nation? Would such a rate structure benefit the eastern railroads, the transcontinental railroads, or any segment of the national economy?

Without a "rate structure which would continue to give mountain-Pacific producers access to eastern markets" there would be no question of divisions, since there would be virtually no transcontinental traffic nor any revenues to divide. The Examiners may call the rate structure "depressed", but if it is as high as the traffic will bear, their characterization has no meaning nor any bearing upon the question how the revenues shall be divided.

Exception No. 12

The second paragraph under "Conclusions" at pages 33 and 34 of the recommended report states as follows:

> "To increase the defendants' divisions 10 percent would have the effect of throwing upon the eastern and midwestern lines most, and in some cases all, of the burden of absorbing the reductions in the interterritorial class rates to and from mountain-Pacific terri- [fol. 968] tory approved by the Commission 5 years ago based principally on improved economic and transportation conditions in that territory. This may be shown by reference to p. 572 of the report in *Class Rates, Mountain-Pacific Territory, supra.* The first-class rate from New York City to Seattle was reduced from $11.72 to $9.38. The present division of the New York-Seattle rates west of the Twin Cities or Council Bluffs is 60.5 percent, which increased 10 percent as

proposed would become 66.55 percent. Applying these two percentages to the respective rates before stated would have given the transcontinental lines a reduction of 85 cents (12 percent), and the connecting lines a reduction of $1.49 (32 percent)."

Argument on Exception No. 12

The Examiners say that the proposal of the defendants would have the effect of throwing upon the eastern and midwestern lines some of "the burden of absorbing the reductions in the interterritorial class rates". What burden? we query. Where is there any showing of burden incurred by the class-rate reductions which were approved by the Commission five years ago? The Examiners arbitrarily select a single *rate, supra,* and proceed to project a percentage relationship (page 34). Without evidence as to revenues received from the class-rate traffic, the rates mean nothing. How much revenue was earned from the class rates prior to the reduction? How much is earned currently? How do these earnings relate to the respective over-all operating revenues? The answers to these questions would at least have to be available before any statement validly could be made concerning "the burden of absorbing the reductions in the interterritorial class rates."

[fol. 969] Exception No. 13

We quote in part from the third paragraph of the conclusions drawn by the Examiners and found on page 34:

"... In the past 10 years it has become clear that the eastern railroads no longer have available to them the profitable volume of freight originating and terminating within their own territorial borders which before World War II caused them to be generally regarded as the strongest group of all American railroads. Accordingly they have become increasingly dependent on interterritorial [sic] traffic, which has grown in importance and stability. About 7 years ago the Commission

found them to be entitled to higher divisions of their interterritorial rates to and from the South and Southwest. Their opponents at that time contended that the troubles of the eastern lines were temporary and would disappear when they realized the full benefits of greater use of diesel locomotives and other improvements. Those predictions were not borne out by later developments, and we are therefore skeptical concerning somewhat similar predictions which have been made in the instant proceedings."

Argument on Exception No. 13

We take exception to the implications involved in the above statement. The Examiners have in effect said that since the eastern railroads have experienced a declining volume of freight originating and terminating within their own territorial borders, they should be given a larger share of the freight revenues accruing from the transcontinental traffic. *This, indeed, is the crux of the matter!* The Examiners have come to no conclusion concerning the relative costs of moving the transcontinental traffic. They have said very little concerning the relative revenue needs of the different carrier groups. But, nevertheless, they propose to strengthen the eastern railroads by giving them some [fol. 970] of the revenues which now go to the transcontinental lines. One begins to wonder if all of the very voluminous evidence in this proceeding was not merely window dressing so that the Examiners might reapportion the divisions in accordance with simple arbitrary convictions not based upon any findings of fact or conclusions of law!

The Examiners might well have advised the eastern railroads to seek traffic more aggressively, to effect greater operating economies, and to increase their efficiencies. Instead, the Examiners state that they are "skeptical" concerning predictions that the troubles of the eastern lines would disappear (page 34). Still, they have not hesitated to advise the western railroads to reduce their "passenger deficits"!

The Examiners conclude their third ordering paragraph as follows: "In our opinion, under the duty of the Commission to consider the requirement of the public interest that all essential parts of the transportation system be maintained, so far as possible, in effective working condition there should be a moderate general increase in the divisions of the eastern railroads." (page 34) Parenthetically, it might be asked whether the Examiners have forgotten that passenger transportation is an essential part of the transportation system. More seriously, however, the Examiners have made no findings nor stated any preliminary conclusions from which it may appear that an increase in the divisions of the eastern railroads is necessary to maintain [fol. 971] any essential part of the transportation system in effective working condition. The opinion of the Examiners, as stated in the sentence last quoted, might as well have been reached prior to the hearings in these proceedings, so far as it can be attributed to any of the evidence of record.

VI.

Findings of the Examiners

Exception No. 14

On page 38 of the recommended report the Examiners make only three findings. The first two are to the effect that the present divisions are unjust, unreasonable, and inequitable; the third is that the new bases of divisions set forth in Appendix B will be just, reasonable and equitable.

Argument on Exception No. 14 and
Proposed Substitute Findings

As pointed out in our exceptions, the bases for the above findings cannot be found in the recommended report and order by the hearing Examiners.

On page 10 of their report the Examiners quote from a decision rendered in 1934, *Divisions of Freight Rates*, 203 I.C.C. 299, in which after stating some shortcomings

in the evidence the Commission stated its conclusions at page 335, as follows:

> "However, this case must be decided on the basis of the evidence of record, voluminous but most unsatisfactory; and there is no other way of deciding it than by the exercise of general judgment after consideration of this evidence such as it is. Upon consideration of all the evidence of record, we are unable to find that the divisions of the transcontinental rates are unlawful."

[fol. 972] In the instant proceedings the Examiners have found the evidence to be voluminous, and clearly it is to them unsatisfactory. They have been unable or unwilling to make findings of fact, and in the end have had to fall back upon general judgment which they might have exercised as well without the evidence. Under such circumstances they should not have endeavored to prescribe far-reaching changes in the transcontinental divisions, which changes cannot but have lasting effects upon the national economy. If the record is beyond their power to analyze, appraise, and reduce to findings of fact, then the exercise of sound judgment permits only one course—the Examiners should say, as the Commission said in 1934:

> "Upon consideration of all the evidence of record, we are unable to find that the divisions of the transcontinental rates are unlawful."

Respectfully submitted,

The People of the State of California and the Public Utilities Commission of Said State, William M. Bennett, Chief Counsel, Cyril M. Saroyan, Senior Counsel, Attorneys for the People of the State of California and the public Utilities Commission of said State, 514 State Building, San Francisco 2, California.

Dated: March 17, 1961

[fol. 973]

BEFORE THE

INTERSTATE COMMERCE COMMISSION

Docket No. 31503 (and Subs. 1-5)

THE AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY, et al.,

vs.

THE ATCHISON, TOPEKA & SANTA FE RAILWAY COMPANY, et al.

TRANSCONTINENTAL DIVISIONS CASE

EXCEPTIONS OF INTERVENORS TO RECOMMENDED REPORT OF EXAMINERS HOWARD HOSMER AND OREN G. BARBER

Public Utilities Commission of Colorado, Denver, Colorado, By: Joseph F. Nigro, Chairman.

Public Utilities Commission of Idaho, Boise, Idaho, By: A. O. Sheldon, President.

Board of Railroad Commissioners of Montana, Helena, Montana, By: William P. Mufich, Counsel.

Public Service Commission of Nevada, Carson City, Nevada, By: J. G. Allard, Chairman.

State Corporation Commission of New Mexico, Santa Fe, New Mexico, By: Ingram B. Pickett, Chairman.

Public Utility Commissioner of Oregon, Salem, Oregon, By: Lloyd Hammel, Assistant Attorney General and Thomas W. Dench, Chief Rate Analyst.

Public Service Commission of Utah, Salt Lake City, Utah, By: Hal S. Bennett, Chairman.

Washington Public Service Commission, John J. O'Connell, Attorney General, Olympia, Washington, By: Frank P. Hayes, Assistant Attorney General.

Dated: March 31, 1961
Due Date: April 5, 1961

[fol. 974] BEFORE THE

INTERSTATE COMMERCE COMMISSION

Docket No. 31503 (and Subs. 1-5)

THE AKRON, CANTON & YOUNGSTOWN RAILROAD COMPANY, et al.,

vs.

THE ATCHISON, TOPEKA & SANTA FE RAILWAY COMPANY, et al.

TRANSCONTINENTAL DIVISIONS CASE

Exceptions to Recommended Report of Examiners Howard Hosmer and Oren G. Barber

Preliminary Statement

By this recommended report the Examiners would find the present divisions of joint interterritorial rates by railroads between points in Mountain-Pacific Territory on the one hand and points in Official Territory and points in Midwestern Territory on the other hand to be unjust, unreasonable and inequitable. The Examiners recommend prescription of a new basis of divisions of transcontinental rates for the future, as set forth in Appendix B of the recommended report. Under the Examiners' proposal separate percentage divisions would be prescribed for each gateway where transcontinental traffic is interchanged between complainants and defendants.

It is impossible to determine from the proposed report and the Examiners make no estimates of the loss of revenue [fol. 975] from transcontinental traffic to be borne by defendants, Mountain-Pacific Lines. Since over half the revenue of these carriers comes from transcontinental traffic, it is obvious from the recommended increases in the per-

centages accruing to the carriers in Official and Midwestern Territory that under the Examiners' proposals there will be a substantial reduction in revenues to the Mountain-Pacific Lines. No precise estimate of revenue loss can be determined without a detailed study of traffic movements via each of the gateways.

Petition for leave to intervene in support of the Mountain-Pacific Lines was filed August 15, 1955 by the state regulatory commissions in Mountain-Pacific Territory, parties to these exceptions. This petition was granted February 7, 1956, by Order of the full Commission. Pursuant to this order, evidence was offered on behalf of intervenors by staff members from these Commissions and by public witnesses representing the major industries and shippers in these Mountain-Pacific states at the Portland, Oregon hearing held May 27 and 28, 1957. The evidence submitted on behalf of intervenors, as well as our interest and position in these proceedings, are discussed in detail in our brief filed June 8, 1960.

The following exceptions are filed by intervenors in support of our position that the expanding economy of Mountain-Pacific Territory requires in the public interest [fol. 976] increased railroad transportation service and facilities. The Mountain-Pacific Lines, who are dependent for over half of their income from the divisions of transcontinental rates, must be able substantially to increase their investments in plant and equipment and improve their service in order (1) to meet their common carrier obligations to the public and (2) to retain their competitive position in the transportation industry. In order to accomplish these purposes additional rather than less revenues are needed by the Mountain-Pacific Lines.

Portions of the recommended report are devoted to a discussion of the comparative costs of operation in the respective territories and to the financial condition of the carriers in the respective territories. While we recognize that a determination of comparative operating costs and financial needs must be made under Section 15(6) of the

Interstate Commerce Act, we took no position as to the merits of the respective claims of the parties on these subjects in our brief and take no position by these exceptions in the controversy between complainants and defendants over territorial operating costs, the merits of the various cost studies or other factors bearing upon the private and financial interests of the participating carriers.

The ultimate conclusions of the Examiners, however, rest not upon the cost and other relative evidence of record but upon their opinions of extraneous economic matters not of record or considered by the parties.

[fol. 977]

EXCEPTION NO. I

Passenger Deficit

Exception is taken to the findings and conclusions of the Examiners on pages 27 to 33 of their proposed report regarding the passenger deficit of defendants. Specific exceptions are taken to the following statements and conclusions of the Examiners:

(1) To the last sentence of paragraph 3 of page 27 reading as follows:

> "Contrary to popular impression, however, in this period the passenger deficit has been larger in the West than in the East, and the eastern carriers have done better in reducing their passenger deficits than the western lines."

(2) To paragraph 2 on page 28 reading as follows:

> "If the rail carriers in the western district had been able to hold their average annual passenger deficit in 1949-1959 to a figure 3 percent less than their 1948 deficit, their revenue saving would have been nearly $82 million per year. The annual saving of the transcontinental railroads similarly estimated would have been more than $60 million per year."

(3) To the last paragraph on page 30 and the first paragraph on page 31 reading as follows:

"The intervening State Commissions share the defendants' concern as to whether those railroads can obtain necessary funds to increase their facilities to the extent necessary to keep pace with the expanding economy of the mountain-Pacific States. One of the interveners' briefs has the following to say on this point:

'In spite of the pressing need for additional investment in equipment and transportation facilities, the mountain-Pacific carriers cannot look to rate increases to provide increased earnings but instead must face further rate reductions. Where then is the money necessary to provide additional facilities, and to maintain the earnings of the Mountain-Pacific carriers to come from? With these carriers [fol. 978] dependent for over half of their freight revenues on these transcontinental divisions, it seems only fair that the Midwestern and Eastern connections, who participate in the transcontinental traffic without having had to make the necessary capital investments at anything approaching the same rate, should be called upon in this divisions proceeding to provide at least a modest increase in the transcontinental divisions accruing to Mountain-Pacific lines.'

"It has already been pointed out in this report that the various changes in the country's freight-rate structure in the past 15 years have not prevented the mountain-Pacific railroads from attaining a greater degree of prosperity as freight carriers than the eastern and midwestern lines. The mountain-Pacific lines, however, are losing relatively much more money than the others on their passenger traffic, and we see no reason for offsetting those losses by increases in their revenue from transcontinental freight. *The obvious answer to*

the question stated in the foregoing quotation is that a reduction in the passenger deficit of the mountain-Pacific lines, which would seem to be imperative sooner or later, should help materially in furnishing funds for additions and betterments. The interveners are in a position to assist in such a course by taking a sympathetic attitude toward discontinuance of unprofitable passenger service. The American railroads other than the defendants in 1959 had a total passenger deficit 15 percent lower than they had in 1948. If the defendants had been able to do as well, they would have had a saving of $67.8 million in 1959." (Italics ours)

These quotations from the Examiners' Report are the fundamental grounds for their ultimate recommendation that the divisions of the Mountain-Pacific lines should be reduced. Apart from this finding as to passenger deficits, no basis is found by them for a reduction in the present divisions, either in the cost evidence or in the financial returns of record. The proposition is advanced for the first time, nevertheless, that the Mountain-Pacific lines' pressing need for an increase in revenues available for additions and betterments, and the claims of the Eastern and Mid-[fol. 979] western roads for higher divisions, may both be met by funds of more than $60 million annually fictitiously created through the reduction in the Mountain-Pacific Lines' passenger deficit. As a basis for the fanciful creation of these funds, the Examiners use the asserted reduction in the passenger deficit of the Eastern roads in a selected period of years as the controlling measure of operating efficiency and regulatory action.

The Examiners, in effect, condemn the Mountain-Pacific roads' handling of their passenger operations, criticize the Mountain-Pacific state commissions' handling of passenger-train discontinuance cases in the past, and admonish our commissions that they should take a more "sympathetic attitude" in the future on applications which may come before them. These directives are grossly unjustified and inappropriate.

The duty of the intervening state commissions, prescribed by the Statutes which they administer, is to act on the record made in each individual proceeding, as does the Interstate Commerce Commission itself in passenger train discontinuance proceedings subject to the jurisdiction of that body.* In their determination in each instance of what is required in the protection of the public interest, interveners are governed by the specific facts of each record, [fol. 980] not by what has been done under different conditions, in some other territory, at some other time.

We recognize that the passenger deficit situation is a serious national transportation problem and every effort should be made to reduce these deficits but such must be accomplished consistently with the public need and the carriers' legal obligations to provide passenger service to the public.

We do not agree that the passenger deficit problem is more severe on the transcontinental western railroads than on other railroads in the nation or that what has occurred in the East since a selected year can be used as a gauge or measure of what can or should be done in another territory under different conditions or that, if it were, the result would be the creation of a fund of $60 million dollars, or any other amount.

Actually, the Mountain-Pacific Railroads since World War II have continuously taken steps to reduce passenger costs and remove unprofitable passenger service, and the state regulatory commissions of Mountain-Pacific Territory have cooperated with these carriers in approving reductions in passenger service consistent with public need.

This charge of excessive passenger deficits and the lack of a "sympathetic attitude" on the part of the Mountain-Pacific state commissions is created by the Examiners in

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* For example by order of Division IV in F.D. 21255 reported on page 103 of Traffic World of Jan. 28, 1961, Southern Pacific Company is required to reinstate in the public interest four passenger trains between Oakland, Cal. and Ogden, Utah.

their report. The intervening state commissions have never been heard on this new passenger deficit issue which has assumed such controlling importance in the Examiners' [fol. 981] conclusions. The state commissions presented their evidence at a hearing in Portland, Oregon, in May, 1957, after all of the carriers had completed their case in chief. At that time, there had been no suggestion of any such charge as to passenger deficits and no such charge was made thereafter on the record. If such a charge is to be extracted from the nebulous passenger deficit controversy and is to be seriously considered in this divisions dispute, the parties are entitled to a hearing on the subject and to offer evidence including but not limited to the facts set forth in the following exceptions.

—A—Reductions in Passenger Service Within Mountain-Pacific Territory

In the first full paragraph on page 31, the Examiners imply that the Mountain Pacific Lines have been lax in taking steps to reduce passenger service to offset losses from that service and further imply that the state regulatory commissions of Mountain-Pacific Territory have not taken a "sympathetic attitude" to the passenger deficit problem and toward the discontinuance of unprofitable passenger service. The Examiners' conclusions on this subject are not in accord with the facts and there is nothing in the record to support their charge.

Because of the controlling weight placed upon the railroad passenger deficits by the Examiners, a study has been made by each of the state regulatory commissions in this territory of passenger train discontinuances in their respective states in order to show the reduction of railroad passenger service in Mountain-Pacific Territory during the [fol. 982] eleven year period 1950 to 1960. Appendix A shows the results of this study. This data is taken from the official records of each of these state agencies.

Each passenger train discontinuance reflects discontinuance of service by one or more passenger trains. Since

this study includes interstate passenger trains, in some instances, the same trains may be included in the report of more than one state. There is no duplication in track mileage discontinued, however, because the distance reported by each state reflects only the mileage in that state. Our study of passenger train discontinuances does not include reductions in commutation service. This study reflects only part of the passenger train discontinuances made by defendants, since it does not include reductions in passenger service made by them on their lines in Western Trunk Lines or Southwestern Territory.

Of the 183 proposals to discontinue service made during the eleven year period, 97 were approved by the state regulatory commissions and an additional 66 discontinuances automatically became effective where the states involved had no jurisdiction over passenger train service or because there was no protest against the discontinuance. In other words, 163 proposals, involving 318 trains, or 89% of the proposed discontinuances became effective. Only 14 proposals or 8% were denied by the state commissions and several of these were approved upon reconsideration. At the end of 1960 there were 6 proposals pending before the state regulatory commissions or before the Interstate Commerce Commission under Section 13(a) to further reduce [fol. 983] passenger train service in Mountain-Pacific Territory.

The number of passenger trains shown as discontinued are based upon one-way train operations. The number of trains reported as discontinued do not include numerous changes in equipment or scheduled service voluntarily made by the carriers during these years. For example, daily train operations in some instances have been reduced to alternate day operations or to a once or twice a week basis. In other cases there has been a down-grading in equipment operated. Some trains which formerly provided pullman and dining car facilities have been reduced to strictly coach trains with or without dining car facilities. The carriers have endeavored to consolidate passenger trains wherever pos-

sible to avoid duplication of service and in some instances the carriers have pooled their passenger train service. On many lines in Mountain-Pacific Territory passenger service has been reduced to one train a day each way. All of these changes result in reduced operating costs.

Appendix A shows that 318 passenger trains were discontinued in Mountain-Pacific Territory between 1950 and 1960. Of these, 208 trains operated in main-line passenger service and 110 trains operated in branch line service.

In this study the number of track-miles in passenger train service discontinued is based upon the railroad distance between points where passenger train service was previously operated. Where train discontinuances resulted [fol. 984] solely in reduction of passenger service over a line but not complete abandonment of passenger train operations over that line, no reduction in track mileage was computed for the elimination of that train. The track mileages reflect actual elimination of passenger train service in each state. Where interstate passenger trains were discontinued only the mileage previously operated within that state was computed.

These statistics from the official records of the state commissions show that defendants have eliminated passenger train service completely on over 5,000 miles of main line service and approximately 4,000 miles of branch line service in Mountain-Pacific Territory between 1950 and 1960. Obviously all costs charged to passenger service have been eliminated from this trackage.

Appendix A conclusively shows that the Mountain-Pacific Lines with the regulatory commissions of this territory cooperating have made substantial progress in alleviating the passenger train deficit in this territory. As a result, defendants have made substantial reductions in their costs for passenger transportation.

In the ten year period, 1950-1960, passenger service has been discontinued completely on over 9,000 miles of line in Mountain-Pacific Territory. There is no excess passenger service left in this territory from which respondents

can substantially reduce their passenger deficit without wiping out passenger service completely in a large part of this territory. The public cannot be denied passenger [fol. 985] service without a determination of the public need for such service as required by state statutes as well as by Section 13(a) of the Interstate Commerce Act.

If the Commission is disposed to consider seriously the passenger deficit issue as a grounds for a change in divisions, we urge that the proceeding be re-opened so that we may offer into the record the relevant facts, including our study of the reduction of railroad passenger train service in Mountain-Pacific Territory between 1950 and 1960.

—B— Passenger Traffic and Revenues

An analysis of railroad passenger traffic and revenues between 1948 and 1959 does not reveal any substantial differences in the decline in railroad passenger service as between the eastern and western districts. (Appendix B)

Miles of road operated in passenger service declined by 13,355 miles in the Eastern District and 29,135 miles in the Western District. Reduction in miles of road operated in passenger service between 1948 and 1959 is 37% for the United States, 39% for the Eastern District and 33% for the Western District. When consideration is given to the longer hauls in the Western District and the greater distances between major metropolitan areas, the reduction in miles of road operated in passenger service is comparable for the Eastern and Western Districts.

A similar analysis of passenger train miles operated shows a decline of 49% between 1948 and 1959 in the Eastern District and 39% in the Western District. Since the [fol. 986] volume of passenger traffic in the east consists of commuter and short-haul coach service, the greater decline in passenger train miles operated by eastern railroads is to be expected and does not necessarily indicate any greater improvement in the Eastern than in the Western District.

An analysis of the number of revenue passengers carried reveals the tremendous volume of passengers handled by the eastern lines in commutation service. Between 1948 and 1959 the number of revenue passengers carried by the eastern railroads in commutation service declined by 90 million passengers or by 37%. During the same years the passenger revenue in the Eastern District from commutation service *increased* by $34 million or 58%. Commutation passengers carried by railroads in the Western District increased by 2 million passengers or 5% between the same years. The western carriers' revenues from commutation service *increased* by $12 million or 120%. The record of the western railroads insofar as commutation service is concerned is better than that of the carriers in the Eastern District.

The number of passengers handled in coach service in the Eastern District between 1948 and 1959 declined by 123 million passengers or 39%. The number of passengers handled in coach service in the Western District decreased by 21½ million passengers or by 49% during the same years. Passenger revenue from coach service in the Eastern District, however, declined by $114 million or 39% while the revenue from coach service in the Western Dis- [fol. 987] trict decreased by only $28 million or 16% during this period. In spite of the greater percentage decline in coach passengers carried, railroads in the Western District had a smaller percentage loss of revenues from that service. The record of changes in coach travel and revenues does not reveal that the railroads in the Eastern District have performed a superior job in the improvement of their passenger situation.

The number of passengers carried in parlor or sleeping car service between 1948 and 1959 declined by 71% in the Eastern District and 65% in the Western District. Comparable declines in passenger revenue from this service are 52% for the Eastern District and 63% for the Western District.

The total number of revenue passengers carried between 1948 and 1959 in all services declined 45% for all Class I railroads in the United States, 47% for the carriers in the Eastern District and only 27% for carriers in the Western District. Comparable declines in total passenger revenues are 32% for all Class I railroads in the United States, 31% in the Eastern District and 33% in the Western District. Irrespective of differences in level of fares and special conditions in the two territories, the record shows that the western carriers' loss in revenues from passenger service is proportionate to that of the carriers in the Eastern District.

There are substantial differences in the nature of passenger service rendered by railroads in the Eastern District than in the Western District. This is reflected in part [fol. 988] by the average distance traveled per passenger. The average distance traveled by passengers in commutation service is substantially the same throughout the United States and varies little from year to year. Passengers carried in coach service in the Eastern District traveled an average distance of 55 to 60 miles between 1948 and 1959 while coach passengers carried in the Western District traveled an average of 190 miles in 1948 and 287 miles in 1959. The coach service of the eastern railroads is concentrated on short-haul passenger traffic while that of the western railroads, especially the Mountain-Pacific Lines, is keyed to serve long distance travelers.

The average distance traveled by passengers in parlor and sleeping cars in the east is approximately 300 miles. Comparable distance traveled in the Western District is approximately 600 miles. Since the Mountain-Pacific lines provide transcontinental coach and first-class passenger service, the average distance traveled by passengers on these lines would be much greater than that of the other carriers of the Western District who operate east of the Rocky Mountains. Obviously this long-haul transcontinental coach and sleeping car passenger traffic is more susceptible to diversion to the airlines than short-haul pas-

senger travel in the east. Time in transit, as well as comparative costs, are important factors affecting the competition for transcontinental passenger travel. Obviously, the passenger deficit problems are not the same in the Eastern and Western Districts.

Analysis of the foregoing passenger traffic statistics does [fol. 989] not support the Examiners' conclusions that the eastern carriers have done a better job in reducing their passenger deficits and that Mountain-Pacific lines can reduce their passenger deficits sufficiently to produce the additional revenues to pay increased divisions to complainants.

In Docket Ex Parte 202 "Increased Fares, Eastern and Western Railroads, 1956", 298 ICC 378, the Commission recognized that both the Eastern and Western lines had substantially improved the efficiency of their passenger train service. The Commission stated:

> "By increases in efficiency, improvements in their service, and experiments with family and other forms of reduced fares, respondents have been able to ameliorate somewhat the impact of these increased expenses. For example, during the period 1948-55, the eastern lines increased their cars per train from 9.05 to 9.47, their average speed from 36.2 to 37.5 miles per hour, and their average miles per locomotive per day from 197.1 to 254.3, while the corresponding figures for the western respondents are 9.22 and 10.05, 37.9 and 42.5, and 265.4 and 397.8. Respondents have also been able to discontinue some of their unprofitable passenger-train mileage, the totals for the eastern respondents being 163.3 million in 1948 and 128 million in 1955, and for the western respondents 163 million in 1952 and 142 million in 1955." (298 ICC 380-381.)

—C— Passenger Fare Increases

By order issued April 30, 1956 in Docket Ex Parte 202, "Increased Fares, Eastern and Western Railroads, 1956",

298 ICC 378, the Interstate Commerce Commission approved general increases of 5% in passenger fares of railroads in the Eastern and Western Districts. As a result of this general fare increase the level of first class fares in the Eastern District was set at 4.725 cents per mile and the level of coach fares was set at 3.544 cents per mile. The [fol. 990] similar level of fares in the Western District was set at 3.675 cents per mile for first-class travel and 2.625 cents per mile for coach travel.

Since the decision of the Commission in that proceeding the railroads in the Western District have increased their first-class and coach fares. Even though the level of fares in the Eastern District may be at a slightly higher level than in the Western District, as previously pointed out, total passenger revenues of carriers in the Eastern and Western District between 1948 and 1959 declined by 31% and 33% respectively. This record contains no evidence from which the Examiners could find that the western railroads have not increased their passenger fares in proportion to their ability to maintain passenger traffic under such increased fares.

—D— Reduction in Costs of Passenger Service

The conclusions of the Examiners that the eastern lines have been more diligent than the western lines in reducing their passenger deficits infers a failure on the part of the Mountain-Pacific Lines to eliminate unprofitable passenger service and to reduce their costs of providing this service consistent with public need.

The Interstate Commerce Commission in numerous proceedings has pointed out that the costs allocated to passenger transportation and reflected in the passenger deficit consist of out-of-pocket costs which can be directly chargeable to passenger service and indirect costs which are allocated on a formula basis between passenger and freight [fol. 991] traffic. In its investigation of the "Railroad Passenger Train Deficit", Docket 31954, 306 ICC 417, the Com-

mission stated on page 420 of its report that only about 75% of the passenger operating expenses as reported can be directly separated from those for freight services. The other 25%, which are not solely related, present a typical problem in the ascertainment of the components of common costs. For the most part the costs which must be apportioned were in the group of accounts for maintenance of way and structures.

The specific rules for the separation of accounts between passenger and freight traffic were prescribed by order of the Commission and became effective January 1, 1953. Under these rules, certain of the common costs between freight and passenger services are allocated according to the unit of service or work performed, such as the gross ton mile, switching locomotive hours, locomotive miles, etc. Other common expenses are apportioned on the basis of a related account or group of accounts which have been separated. General office and traffic expenses are included among the accounts allocated in this manner.

The Commission, by decision in the investigation of the passenger train deficit, (306 ICC 417, 427) pointed out that "the separation rules do not reflect, nor are they intended to provide, the cost of operating individual trains; they are not intended to determine the expenses which would be avoided if all passenger services were discontinued; and they are not intended to measure the elusive 'out of pocket costs'".

[fol. 992] The Interstate Commerce Commission, in interpreting Section 13(a) of the Interstate Commerce Act has consistently held that joint costs which are apportioned between freight and passenger traffic cannot be considered in abandonment proceedings, since these costs will continue in effect irrespective of passenger service. In Docket 20638, Chicago & Northwestern Ry. Co., Discontinuance of Service between Minneapolis, Minn., and Council Bluffs, Ia., 307 ICC 463, the Commission held on page 471 that alleged reductions in costs for general expenses, which included salaries and expenses of general officers, must be disregarded

in determining the expenses properly attributable to those trains. Similarly, expenses for maintenance of way and structures were disallowed for the purposes of that report, on the grounds that neither these items of expense can properly be classified as avoidable costs and therefore they have no bearing in determining the actual costs of providing the service to be abandoned. Similar findings were made in Docket 20861, Chicago & Northwestern Ry. Co. Discontinuance of service between Chicago, Ill. and Council Bluffs, Ia., 307 ICC 775, 778, and in all cases under Section 13(a) thus far decided by the Commission.

Pursuant to the Commission's rules governing the separation of operating expenses between freight and passenger service, the Mountain-Pacific Lines obviously charge a substantial sum for maintenance of way and structures, traffic and general expenses of their transcontinental lines to transcontinental passenger service. The Examiners have [fol. 993] not shown what these joint costs are or to what extent the joint costs presently borne by the transcontinental passenger service would be allocated to freight service if passenger service were discontinued and the effect of such a transfer of costs on their earnings from freight service.

The Examiners nevertheless conclude on page 31 of the proposed report that if the defendants had been able to do as well as other railroads in their districts, they would have had a saving of $67.8 million in 1959. There is no indication by the Examiners how the transcontinental western railroads are to accomplish this feat. Indeed, the Examiners entire theory is utterly unrealistic and entirely inconsistent with this Commission's administration of train discontinuance cases.

The controlling test in train discontinuance cases is *not* whether there is a statistical passenger deficit but, instead, whether a given train is meeting its out-of-pocket expenses and whether the public need requires the continued operation of the train. The fatal defect in the Examiners' con-

clusion is that it is based entirely upon statistical passenger deficits without any showing whatever that there is any substantial amount of passenger train service being performed by the Mountain-Pacific lines as to which discontinuance would be permitted by the Commission under Section 13(a) of the Act. Even if there were such service to any appreciable extent, the Examiners would also have to find that a similar degree of savings could not be realized by train discontinuances in the East. In view of the standards established in the Commission's own train discontinu- [fol. 994] ance cases, it is not only speculative but beyond belief that actual dollar savings of $60 million annually or any substantial sum is available to the Mountain-Pacific lines relative to the Eastern lines.

In its conclusions to the passenger deficit investigation Docket 31954, 306 ICC 417, the Commission pointed out on page 479 that the causes of the railroad passenger deficit are many and complex; no single one more culpable than any of the rest. In the same way the problems of controlling the passenger deficit must be tackled step by step. It has been handled by respondents and by the state regulatory commissions in that manner for more than 10 years and should be so handled in the future.

The Examiners erred in their conclusions regarding the ability of the Mountain-Pacific Lines to produce from reductions in their passenger deficits the money to pay any increased divisions of transcontinental freight rates to complainant Eastern and Midwestern Lines.

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